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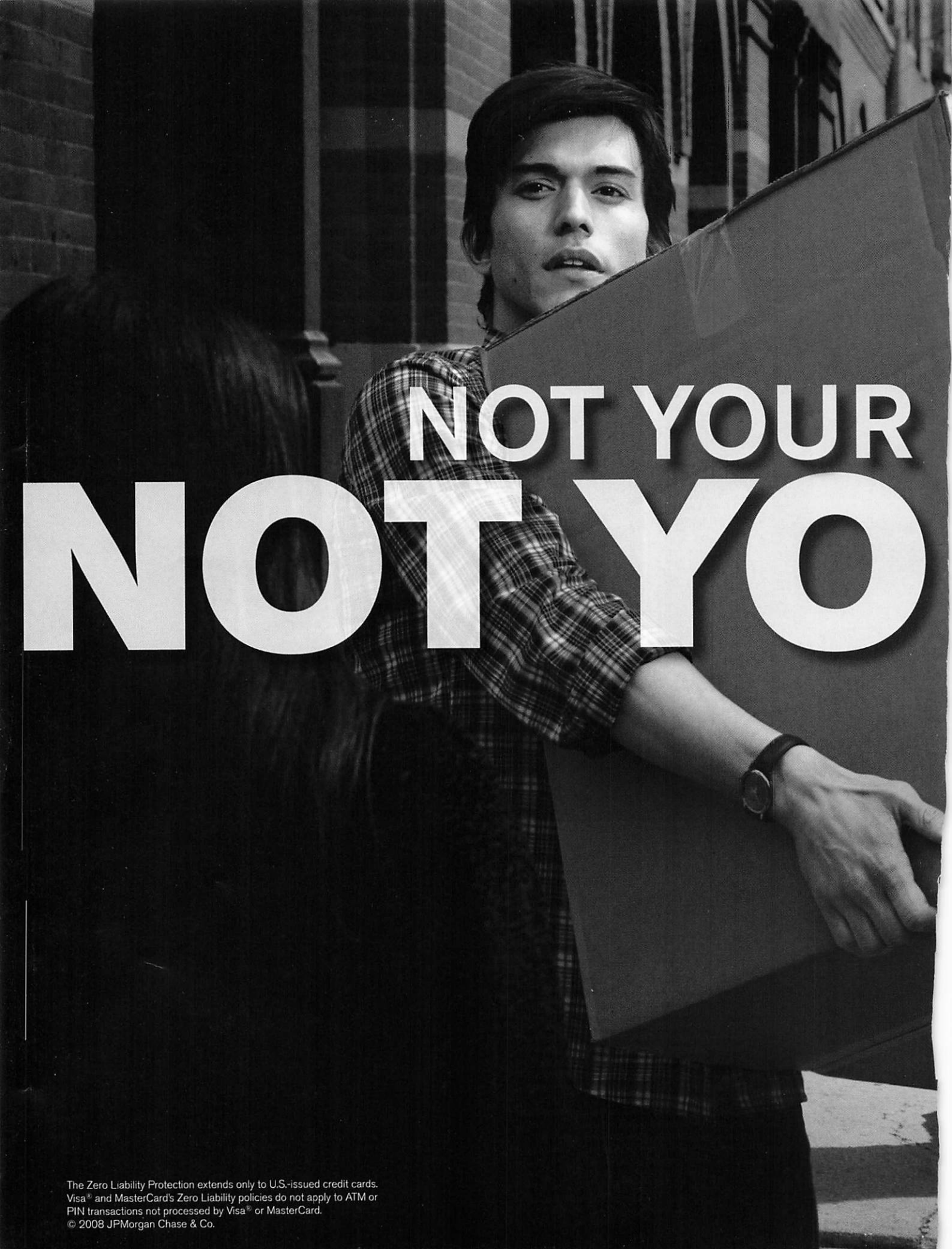
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Turning a Hobby into a Lucrative Venture

Selling homemade treats may seem like a simple business, but for bakery founder Nicole Mahler, making smart legal decisions has been the key to entrepreneurial success.

Mahler, 35, started making cupcakes at her home in Schaumburg, Ill. to keep busy after leaving her marketing job in 2005 and getting pregnant. By the time she delivered a little brother to her 14-year-old son, she had also birthed an idea for a business.

Encouraged by a friend, Mahler perfected her recipes so that her products had an extended shelf life. Last July she created a storefront on Etsy.com, an online marketplace for handmade products. Mahler leased a commercial bakery, where she prepares the cupcakes, to ensure that she meets government food-safety standards. She set prices that seemed fair to her: The popular PB & J Sandwich Cupcake, an eight-ounce creation, for instance, sells for \$6.50. She named the store Bangerang Bake Shop.

To protect her personal assets, she incorporated and insured the business. She also wanted to safeguard her ideas, so she turned to James Hultquist, a partner in the Chicago office of the law firm Reed Smith. He protects intellectual property for both corporate and small-business clients.

James Hultquist: *"When startup companies have new or very unique ideas, protecting their intellectual property should be high on the list. A lot of times, entrepreneurs don't do that early on, and it costs them money later if someone tries to copy their ideas."*

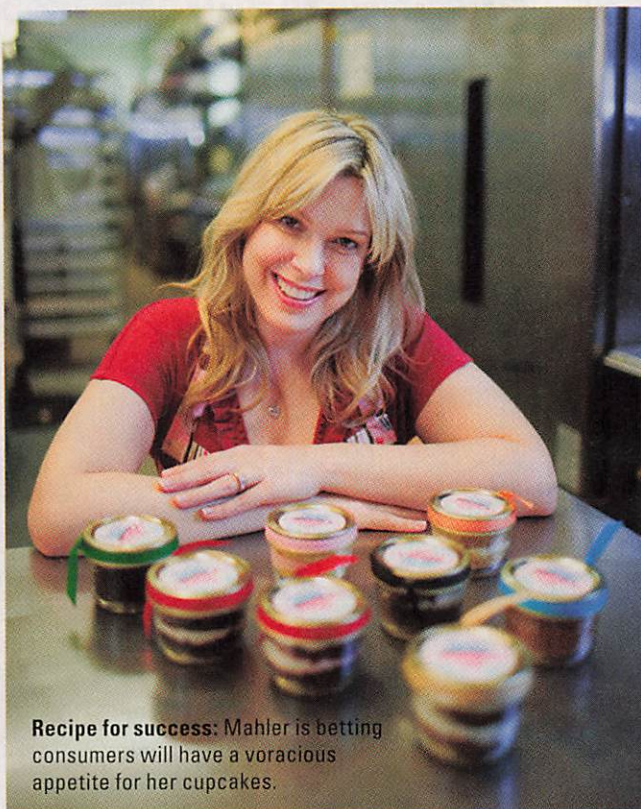
Hultquist's first step was to find ways to protect one of Mahler's ideas: shipping the cupcakes in Mason jars.

Nicole Mahler: *"I wanted to mail them without spending an arm and a leg on shipping. I saw some Mason jars and the idea just clicked. No one else is doing it."*

Hultquist also suggested that she conduct a trademark search to protect the brand identity of her company.

Hultquist: *"You don't want to get too far down the road in using your name in commerce and find that another company that does business in your space has a similar one."*

Thanks to Etsy's high traffic, Mahler's bakeshop grew faster than she had ever imagined. She found herself in the kitchen 13 to 16 hours a day to keep her store stocked with her 32 flavors. Mahler is now planning a freestanding website to use as her main marketing venue until her revenue grows. She has also gotten some free publicity from blogs for cupcake lovers.



Recipe for success: Mahler is betting consumers will have a voracious appetite for her cupcakes.

Tom Maday

Hultquist: *"Doing business on the web clearly provides a market that might not otherwise be available to you."*

Now Mahler is confident about expanding her business. She is already shipping cupcakes internationally to such countries as Australia, Japan, and Singapore. Some customers have sent them to soldiers in Iraq. After racking up \$15,000 in sales in February, she is now looking at buying her own bakery and equipment so she can grow the company to about \$100,000 in sales within a year.

Mahler: *"Right now, there's no way of keeping a very large quantity of cupcakes in my shop, because the business has gotten so big."*

—E.M. Sicoli

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Sarah: saw Bob today.

Dave: heard his father passed. so sad. did Bob and Sue take over the house? that was the plan.

Sarah: no, they had to sell. estate taxes.

Dave: man...

Sarah: so, what would happen to mom's house?

Dave: |

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Another Reason Simpler Is Smarter

LAST YEAR SEVERAL MUTUAL FUNDS I OWN PAID OUT fat dividends and capital gains. In a lackluster year for returns, you'd think that would make me happy. It doesn't. As I write this, I've just finished filing my taxes, and I'm still smarting at how much higher my bill was thanks to those distributions.

As you know, a mutual fund must pass through to its shareholders essentially all the dividends and net capital gains it earns. If you hold your shares in a regular taxable account, you owe taxes on the money the fund pays you—even if, like most investors (including me), you plow it right back into the fund. And here's where it gets really aggravating: A fund can realize abundant gains and still have a losing year overall. **T. Rowe Price Small Cap Value** (ticker symbol: PRSVX), a MONEY favorite that I've owned for years, had a slightly negative 2007 but paid out distributions that equaled 12.5% of its year-end value.

Manager Preston Athey explains that he was merely doing his job, and rather well: Private equity or corporate buyers announced takeovers of 33 companies in the fund's portfolio. "If you have to distribute gains," Athey says, "this is how you want it to happen." And most of the payout qualified for the 15% tax rate. Yet because the fund's unrealized losses more than offset those realized gains, I ended up making no money on the fund but still paying Uncle Sam taxes equivalent to almost 2% of my stake. Don't mention it, Uncle.

I was hardly alone. U.S. funds set a record for capital-gains distributions last year at \$582 billion. One reason, according to Tom Roseen, a senior research analyst at fund tracker Lipper, is that the tax losses funds had been carrying since the 2000-02 bear market (and had been netting against subsequent gains) were used up. "Shareholders had been enjoying a tax holiday," he says. "That ended last year." The typical fund, Roseen says, loses nearly two points of return to taxes on distributions each year.

How do you plug this leak? One way is to construct the kind of portfolio outlined in this month's cover story, "The Only Seven Investments You Need." Index funds, which make up the core of our simple septet (and the bulk of my portfolio too), are tax-efficient by nature. Since they aim to replicate an established index, they do little of the buying and selling that turns unrealized gains into taxable realized ones. Investors in the **Fidelity Spartan 500 Index** (FSMKX) fund, for example, have surrendered just three-fifths of a point of return, on average, for each of the past 10 years. Careful asset location—the other key feature of our



simple strategy—also helps minimize the tax drag. The idea is to use tax-deferred retirement accounts such as IRAs and 401(k)s to hold stock and bond funds that distribute a big portion of their taxable return each year.

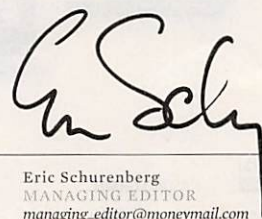
To be honest, tax efficiency wasn't the first priority for the



Simplicity, diversification, cost and potential return were the criteria for choosing the seven-fund portfolio for our cover story. Still, if **keeping it simple helps you keep more gains away from the IRS**, what's wrong with that?

story's two lead authors, editor-at-large Michael Sivy and contributing writer Carla Fried, despite their boss' bellyaching. Simplicity, diversification, low cost and high potential return were their main criteria. Still, if keeping it simple helps lower your tax bill—and it does—what's wrong with that?

I'd be remiss if I didn't also mention this month's real estate special report, which starts on page 80. Editor-at-large Pat Regnier, senior writer Stephen Gandel and writer-reporter Amanda Gengler offer sharp insight into a market that's still working off nearly a decade of excesses and is about to undergo wrenching change. If you own a home, this is a must-read.


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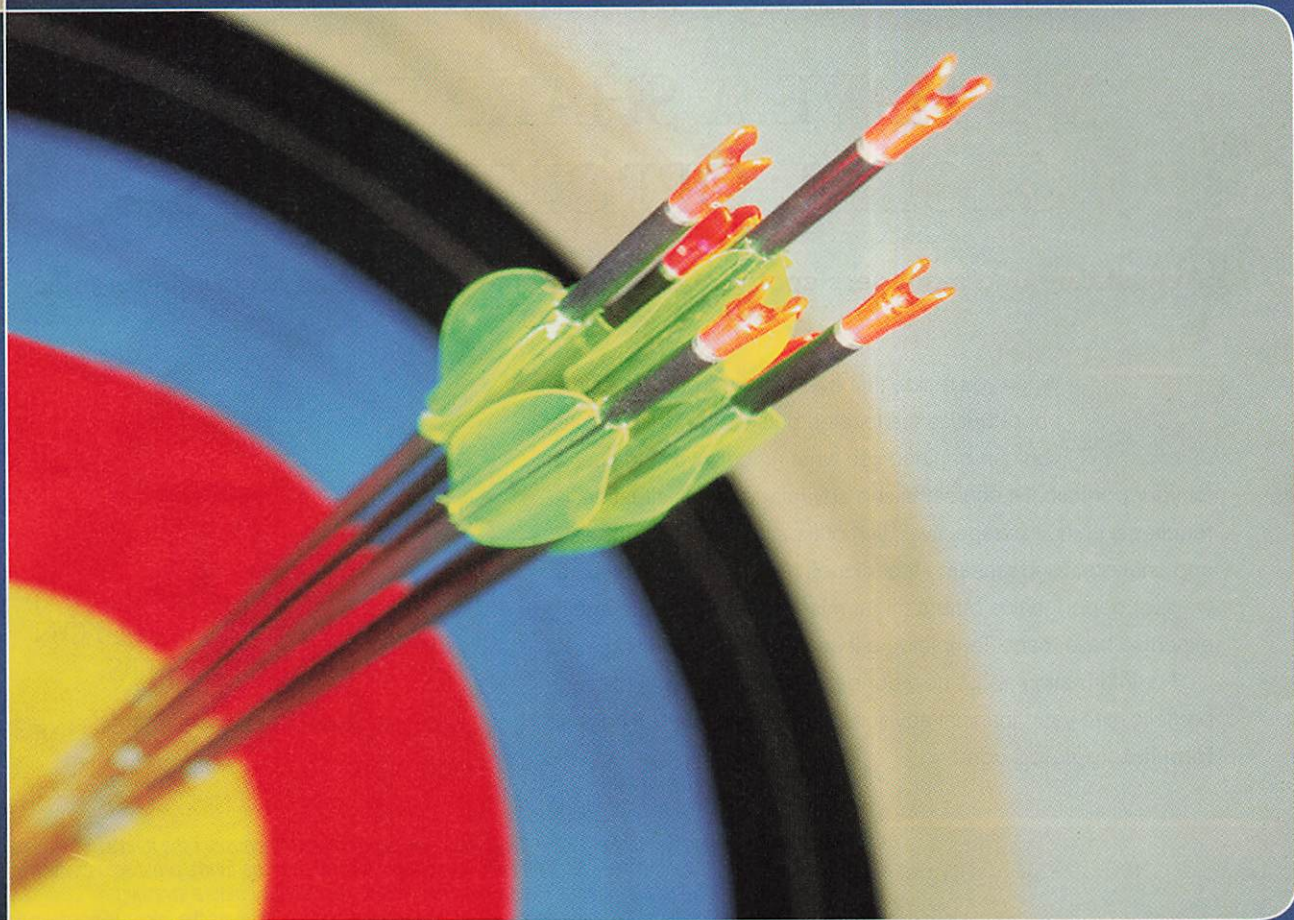
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†Source: Morningstar® 2/29/08. For each fund with at least a 3-year history, Morningstar® calculates a risk-adjusted return measure that accounts for variation in a fund's monthly performance (including the effects of all sales charges), placing more emphasis on downward variations and rewarding consistent performance. The top 10% of funds in each category receive a Morningstar Rating™ of 5 stars, the next 22.5% receive 4 stars, the next 35% receive 3 stars, the next 22.5% receive 2 stars and the bottom 10% receive 1 star. (Each share class is counted as a fraction of one fund and rated separately.) The Fund was rated against 180, 155 and 109 funds and received Morningstar Ratings of 5, 5 and 5 stars for the 3-, 5- and 10-year periods, respectively. Morningstar Rating™ is for Class A shares only; other share classes may have different performance characteristics. ©2008 Morningstar, Inc. All rights reserved. The information contained herein is proprietary to Morningstar and/or its content providers; may not be copied or distributed; and is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information.

T. Rowe Price Retirement Funds:

The "best target-date retirement funds"

Kiplinger's, November 2007



Important factors to consider when planning for retirement include your expected expenses, sources of income, and available assets. Before investing in one of these funds, weigh your objectives, time horizon, and risk tolerance. The funds invest in many underlying funds and are exposed to the risks of different areas of the market. The funds assume a retirement age of 65.

Just choose the year closest to your expected retirement date:

Fund Name	Morningstar Rating [†]	Fund Name	Morningstar Rating [†]
Retirement 2010 Fund (TRRAX)	★★★★★	Retirement 2035 Fund (TRRJX)	★★★★★
Retirement 2015 Fund (TRRGX)	★★★★★	Retirement 2040 Fund (TRRDX)	★★★★★
Retirement 2020 Fund (TRRBX)	★★★★★	Retirement 2045 Fund (TRRKX)	Not Yet Rated
Retirement 2025 Fund (TRRHX)	★★★★★	Retirement 2050 Fund (TRRMX)	Not Yet Rated
Retirement 2030 Fund (TRRCX)	★★★★★	Retirement 2055 Fund (TRRNX)	Not Yet Rated

Past performance cannot guarantee future results. The Overall Morningstar Rating™ is derived from a weighted average of the performance figures associated with a fund's 3-, 5-, and 10-year (if applicable) Morningstar Rating™ metrics. The Retirement 2010 Fund was rated among 129, 129, and 45 target-date 2000-2014 funds; the Retirement 2015 and 2025 Funds were rated among 118 and 118 target-date 2015-2029 funds; the Retirement 2020 Fund was rated among 118, 118, and 31 target-date 2015-2029 funds; the Retirement 2030 and 2040 Funds were rated among 152, 152, and 42 target-date 2030+ funds; and the Retirement 2035 Fund was rated among 152 and 152 target-date 2030+ funds for the overall, 3-year, and 5-year periods ended 3/31/08, respectively. Ratings are based on risk-adjusted performance. Request a prospectus or a briefer profile; each includes investment objectives, risks, fees, expenses, and other information that you should read and consider carefully before investing.

Kiplinger's magazine said T. Rowe Price has "the best target-date retirement funds" based on low fees and high allocation to stocks. When you dig deeper into your investment options, it's easy to understand why more and more investors are choosing T. Rowe Price. The higher a fund's allocation to stocks, the greater the risk.

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SAVE YOUR INVESTMENTS, SAVOR YOUR WINE

"The Best Ways to Protect Your Money Today," the first story in May's cover package, *The 100 Best*, is a great help, as it condenses all the information I have been desperately trying to find in one easy-to-read article. I look forward to future stories in *MONEY* that help an average person like me protect against the extraordinary amount of volatility and uncertainty that characterize today's world.

SEAN LIU *Austin*

Your first annual Best List is so valuable that I bookmarked it on CNNMoney.com for future reference. The segment **"The Best Wines for Under \$20"** was particularly useful. We found the Escudo Rojo wine for \$13 locally and gave it a try (the most apt word for it: elegant!), and we've also purchased a bottle of the Sebastiani Merlot that you recommended. Great picks!

TOM EGAN *Berlin, Conn.*

CARE PACKAGE

"Take Charge of Your Health Care" [April] is very well written and educational. With health costs rising, understanding one's options is important for maintaining affordable coverage without compromising quality of care.

TOM DIXON *Richmond*

FORWARD MARCH

Thank you for your story on a special man, 1st Lieut. Ivan Castro [**"A Soldier's Story,"** April]. After I read it, I made copies for the brokers where I work to share this story of a true winner. And I'm now more grounded: Whenever I catch myself complaining about traffic or the market, I remind myself of the amazing drive and perseverance that Castro demonstrates.

ERIC NICHOLS *Rolling Hills, Calif.*

I greatly appreciated your story about 1st Lieut. Ivan Castro. Despite his undergoing horrific personal injury and painful rehabilitation, this hero desires only to continue serving his country. After 18 years of service, he deserves the honor of being allowed to finish his commitment in whatever capacity he is able. Anything less than that is a shameful indignity.

CAPT. PAUL NICHOLAS, U.S. MARINE CORPS
Monterey, Calif.

ALL PLAY AND NO WORK?

I agree that it's important to be flexible in the rate of withdrawal from one's retirement account [**"One Safe Harbor That's Riskier Than You Think,"** The Long View, April]. But given that Americans already work so hard, your suggestion of continuing to work (even part time) isn't my idea of enjoying retirement.

JAMES LEE ROBERTSON *Vicksburg, Miss.*



WELCOME TO THE JUNGLE

Your selection of Costa Rica as a reasonably priced vacation place was right on [**"The Best Places to Vacation,"** May]. My wife and I just returned from a tour, and the volcanoes, rain and cloud forests, and jungle rivers and lodges made it one of our most interesting trips!

JIM KING *Charlotte, N.C.*



Ivan Castro's determination is incredible [**"A Soldier's Story,"** April]. It's stories like this, which **tie the human element to financial issues**, that make *MONEY* the most helpful magazine I've ever subscribed to! —Bob Berube, Park City, Utah

A COUPLE ON THE SAME PAGE

Planning for my wife's retirement should she outlive me is a potentially gloomy subject, but April's **"She's Cute. She's Smart. She's My Future Widow"** [The Bottom Line] uses humor masterfully to address it. I've shared the column with friends as well as my wife. After she read it, my wife said that women should just leave the page folded open so their husbands can't miss it. And I just realized—that's how I came across it!

ANDREW LONGO *Nutley, N.J.*

Re: the statement that "Americans now have about a third more buying power," I would point out that Costa Rica's tourist industry adjusts prices in light of the exchange rate. Many things that cost 360 colones five years ago will cost 500 colones today...meaning \$1 then, \$1 now.

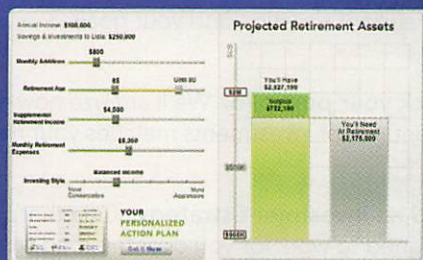
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THREE REASONS TO FEEL OPTIMISTIC

Yes, it's a sour market. But that means it's also a good time to make lemonade.

➤ The S&P 500 has tumbled 12% since October; the real estate meltdown is weighing on the economy; and most of us are just trying to preserve what we've got. You can do more than survive, however. It's often the bleakest moments that present the richest groundwork for gaining wealth. "People who stay optimistic in rough times generally do far better in their investing over the long run than those with a bunker mentality," says Chris Kimball, a financial planner in Lakewood, Wash. What you need to know in order to squeeze good results from bad times:

➤ **There must be bargains out there because the value vets are back in the hunt.** A trio of venerated value-oriented mutual funds have recently reopened to outsiders: Dodge & Cox Stock (DODGX), Longleaf Partners (LLPFX) and Royce Opportunity (RYPNX). Good news for you. Six months after the S&P tanked during the past recession in 2001, all three funds were ahead of the index by at least 4.5 percentage points.

➤ **It's a cheap time to convert a traditional IRA into a Roth.** Your balance has likely shrunk, so you'll pay less tax on the conversion. If you're down by 12% on a \$50,000 portfolio, you'll save \$1,680 in taxes if you convert now, assuming you're in the 28% bracket. But the greatest benefit is that once you retire, you won't pay *any* tax on withdrawals. The caveat: You can't convert if your income is too high (roughly \$100,000, married or single).

➤ **The bad times for stocks will be over before you know it.** The nine recessions since the early 1950s had a median length of 10 months; three of the past four lasted eight months or less. And stocks typically start to recover about halfway through an economic slump, averaging a 13% gain over the second half. So hang tough. By the time a recovery looks like a sure thing, it'll be too late to catch the big bounce. —GEORGE MANNES

EXPERT OPINIONS

The Pros' Best Advice For New College Grads

ON CAREER

"Clean up MySpace and Facebook pages because potential employers will check them. One test: Make sure there's nothing up there you wouldn't want your grandmother to see."
—Alexandra Levit, career counselor and author, *How'd You Score That Gig?*

ON SPENDING

"Make it a habit to have more money coming in than going out. You may need to drive your clunker a bit longer or postpone that trip to Europe." —Brian Jones, wealth adviser and author, *Getting Started: The Financial Guide for a Younger Generation*

ON SAVING

"Sign up for your 401(k) the first day on the job; and put \$25 a month in an ING Direct savings account as a cash cushion. Don't let credit cards or Mom and Dad be your emergency fund." —Sheryl Garrett, financial planner and founder, Garrett Planning Network



FINANCIAL PLANNING

WHAT YOUR ADVISER WILL NEVER ASK

You may think you have a frank relationship with your financial planner. But a new survey suggests that a vast majority of clients and advisers—some 98% in fact—have a hard time talking about even basic issues (such as how long you're likely to live, what health problems you could have and when your cash will run out). As a result, that plan you thought would provide lifelong security may be based on erroneous assumptions. After all, if your C.F.P. built a strategy assuming you'd live till 95 while your Granny lived to 115, you're taking a big risk. Lesson: If your planner doesn't bring up these topics, you should. —JOE LIGHT



TABOO TOPICS

Percentage of planners and clients who dislike discussing:

Life expectancy
55%

Health-care issues
53%

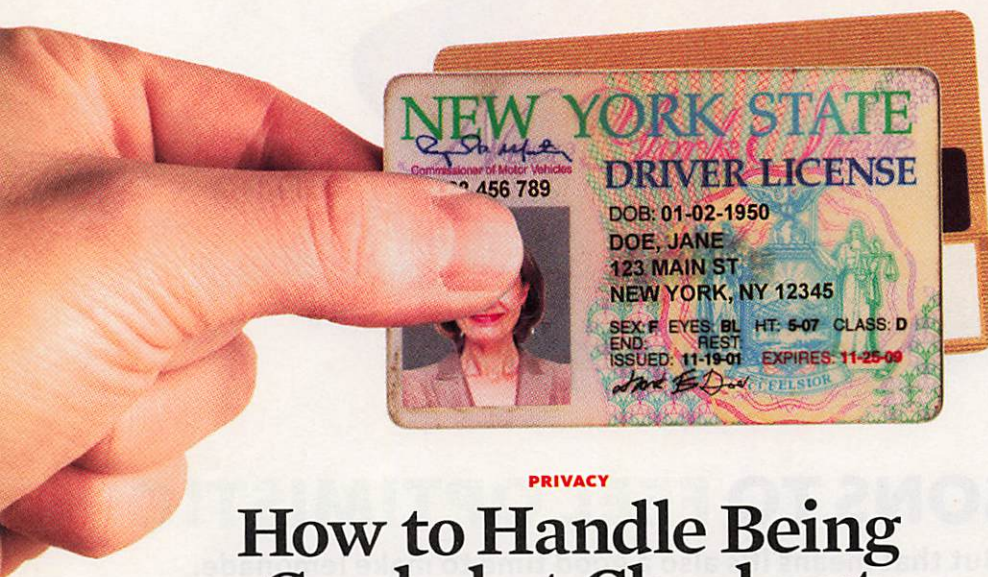
Years savings will last
34%

Legacy planning
34%



SOURCE: MFS Investment Management.

Getty (cap); Corbis (hand)



PRIVACY

How to Handle Being Carded at Checkout

Give a store clerk your credit card, whether for a latte or a laptop, and you may increasingly be asked for ID too, says security analyst Rich Mogull. "Retailers see it as a way to curb losses from fraud," he explains. But think twice before handing over your license. The information on it—combined with your credit-card number—can be a bounty for an unscrupulous employee; less risky but annoying, the store may use it to put you on mailing lists. Plus, since major card issuers won't hold you liable for fraudulent charges, being forced to show ID doesn't give you any extra protection. If you're asked:

REFUSE MasterCard, Visa and Discover actually forbid stores from requiring ID with a signed card; AmEx discourages the practice. Let the clerk know this. Print the clauses from MC's and Visa's merchant agreements at privacyrights.org/ar/Alert-FS15.htm; carry them in your wallet.

CALL FOR BACKUP Reach MasterCard's emergency hotline at 800-MC-ASSIST; Visa at 800-VISA-911; Discover at 800-DISCOVER. A rep may be able to convince the clerk, but if not, at least issue a complaint. Rogue merchants can be fined or suspended.

PAY WITH PAPER If all else fails, use cash—it's risk-free. —ANTHONY CITRANO III

...Keep off the grass U.S. households spent an average of **\$428** on lawn and garden products in '07, says the National Gardening Association...



3
THINGS
TO KNOW
ABOUT

Funding Your Candidate

As November draws nearer, expect a barrage of pre-recorded phone calls and other pleas from presidential hopefuls who want your vote—and your financial support. Already the candidates have raised nearly as much as their counterparts did in the entire 2004 race, with several months still to go. Before you lend a hand to a pol, keep these facts in mind.

➤ **You can give only so much.** For 2008 you can donate \$2,300 to a candidate per primary and \$2,300 per general election; \$28,500 to a national party; \$10,000 per state or local party; and \$5,000 per political action committee (PAC). (The limits are adjusted every two years for inflation.) You can give limit-free to a 527, a thinly veiled candidate lobby group lightly regulated by the Federal Election Commission (FEC). Example: the anti-Kerry Swift Boat Veterans for Truth from '04.

➤ **Your info will go public.** As a result of post-Watergate reforms, whenever you make a campaign contribution, you have to provide your name, job, employer and address. Once your 2007-08 contribution to a candidate, party or PAC exceeds \$200, that campaign must pass your info to the FEC, which posts it on FEC.gov. Sites like OpenSecrets.org and FundRace.org then display it in searchable databases. If you give \$200 or less, the campaign doesn't have to report it to the FEC.

➤ **You won't get any thanks from Uncle Sam.** No matter whether the donation is to a candidate, a PAC, a party or a 527, you can't take a federal tax deduction for it. If you want a write-off, give instead to a charity your candidate supports. If you like the Democrats' plans for universal health care, you might give to Physicians for a National Health Program. Or, if you oppose tighter gun control, you could contribute to the National Rifle Association Foundation. —JOE LIGHT

WHAT
THE
HECK
IS
AN

Actively Managed ETF?

DEFINITION: An exchange-traded fund—a fund that trades like a stock—in which the manager tries to outperform the market by strategically trading stocks and bonds. This stands in contrast to a traditional ETF, which tracks a market index.

The term entered the financial vernacular in March, when Bear Stearns rolled out the first product of this type, an ultra-short bond fund with the ticker symbol YYY (perhaps echoing the cries of the troubled firm's investors). PowerShares and Vanguard are launching similar products.

These newfangled funds probably won't offer the benefits of traditional ETFs—fees as low as 0.07% and a small tax bite thanks to infrequent capital gains. (The Bear fund has an expense ratio of 0.35%.) What's more, there's no guarantee that they will deliver the anticipated above-average returns. After all, the new ETFs will face the same challenges as actively managed mutual funds, more than half of which underperform the market over time. —JOE LIGHT

USED IN A SENTENCE: "There's no reason to rush into **actively managed ETFs**. It pays to stand back and take measure of how they perform first." —JEFFREY PTAK, DIRECTOR OF ETF RESEARCH FOR MORNINGSTAR

...Pennies in the piggy bank Less than one in three Americans put away at least 10% of income, per the American Savings Education Council...



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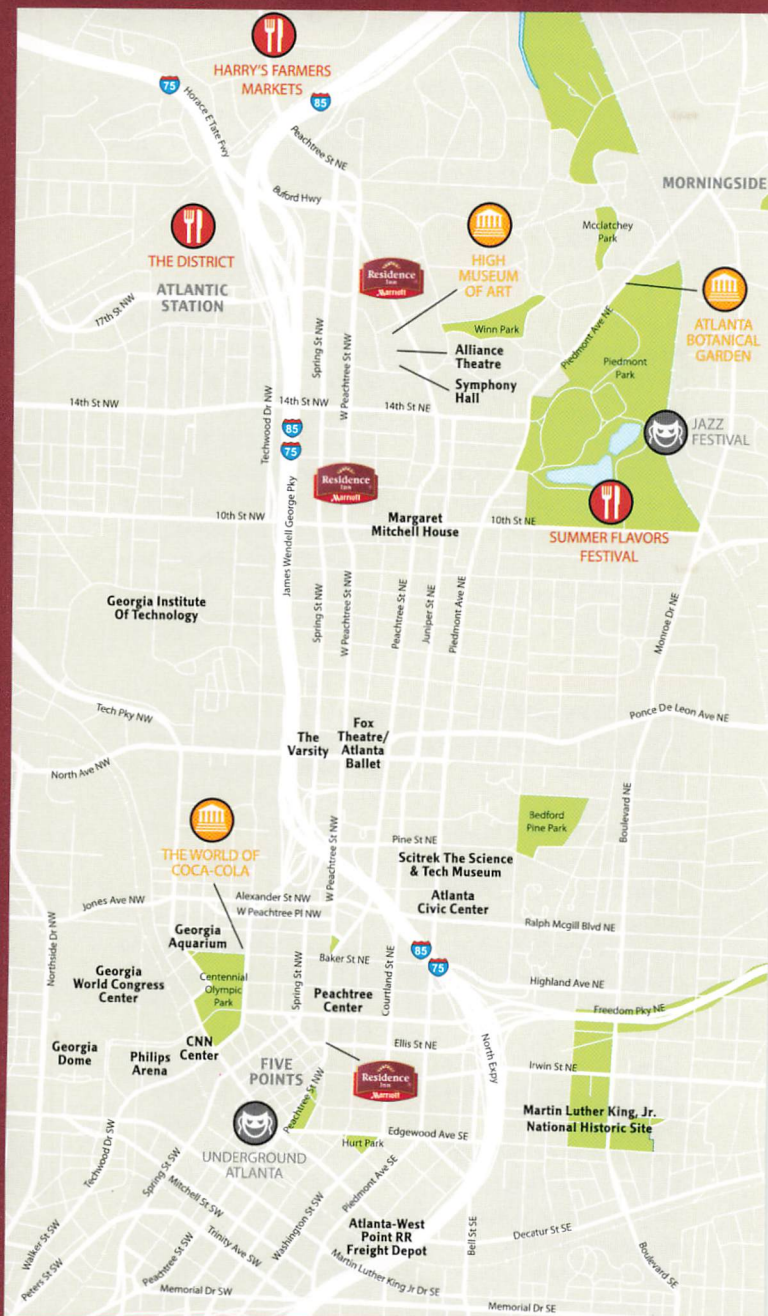
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“Do I have to pay \$150 to cancel cell service that doesn't work?”



Q I signed a two-year contract with Sprint for my cell phone. A year and a half later, I moved to a new home a few miles away in the same city. **I can't seem to get a signal inside my house,** which is a problem since I don't have a landline. Sprint told me to upgrade the software on my phone, but that didn't help. So I switched to Verizon—and now get perfect service in my home. But am I stuck with Sprint's \$150 cancellation fee? —Dan B. Lindeman III, Fort Thomas, Ky.

Answer It's not *impossible* to get out of a cell-phone contract without paying an early-termination fee—it's just that historically, carriers have made it incredibly difficult. Ever since cell phones were invented, wireless providers have tried to lock in customers by wooing them into long-term contracts and levying fees as steep as \$250 if they cancel before that contract is up.

Among the few viable excuses to get out of a contract penalty-free are death, active military duty and...relocation, if you can prove that your new area doesn't get adequate coverage. To make that case, call the carrier and have the rep look up the number of cell towers in your neighborhood; if the carrier determines it isn't enough, you may get a dispensation. You can also ask to have someone test the signal up to your driveway. But carriers won't guarantee service inside your home. “There are too many factors out of our control,” says Sprint spokesperson Roni Singleton. (For example, a construction material like granite can block a signal even with multiple towers nearby.)

»TIP
Most carriers allow you to test-drive their service. Even if you sign a contract, you can cancel without penalty if you have a service problem within 30 days.

Singleton says Sprint has five towers in your area. Bummer—no free pass this way.

But these days even if you can't get out for free, you may at least be able to shave

some money off that exit fee. In 2006, Verizon announced that it would prorate its penalty. AT&T followed, and late last year Sprint joined the pack. The company is still working out the details but plans to enact its policy later this year. (With AT&T, which clips \$5 off \$175 for every month served, your final charge would've been \$75 since you stayed 15 of 24 months.) We asked Sprint to make an early exception for you. Since the terms of the policy aren't defined yet, Singleton went one better and offered to waive the whole \$150 instead. Good call. \$



SO FAR MONEY HELPS HAS SAVED READERS

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? Having a financial nightmare? E-mail Donna Rosato at money_helps@moneyemail.com. And post your comments about this column at cnnmoney.com/moneyhelps.

Start



Behind the Buzz

Starbucks Bucks Are card perks too good to be true?

THE BUZZ America's most ubiquitous caffeine dealer has been losing ground lately to fast-food rivals like Dunkin' Donuts and McDonald's. To win you back, Starbucks just unveiled a series of perks: Free refills on drip coffee! Free syrup shots and milk substitutions! Free drink with bean purchase! Free Wi-Fi! All you have to do: pay with a prepaid Starbucks Card, which holds up to \$500.

THE TRUTH Maybe you've given a card as a gift before? These extras are meant to coax you to front-load one for yourself so Starbucks can guarantee sales. Not that the benefits are bad. The refills are sweet; upgrades save up to 70¢ a drink; and the Wi-Fi, which makes its debut this summer, is handy, if stingy (two hours a day vs. unlimited use at chains like Cosi and Panera Bread). The 'Bucks card *can* save bucks for regulars. Just don't load it with more than you'd spend otherwise. And when registering it online, opt out of mailings from the store and “carefully selected” partners.

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—ISMAT SARAH MANGLA

...The old-fashioned way works! 69% of Americans with more than \$500,000 in assets earned their fortune vs. inheriting it, reports PNC...



the big idea ELIZABETH WARREN

Crusader Against "Gotcha" Banking

This Harvard Law prof wants Uncle Sam to keep lenders from screwing you INTERVIEW BY DONNA ROSATO

> Your credit-card terms are usurious; your mortgage contract disguises the real cost of your home; and you need a magnifying glass to catch all the fees in your auto loan. As a result, you may be paying thousands more than you should for these products, says Harvard Law professor Elizabeth Warren. She's long made it her job to shine a light on the worst practices of the financial services industry—before Congress, on the blog *CreditSlips.org* and in her bestseller *The Two-Income Trap*. Now she's calling for a new watchdog agency to oversee financial products. And with support from at least one presidential contender, the idea is gaining some traction.

Q. You are proposing a Financial Product Safety Commission to protect consumers. How would it work?

A. It would function much like the Consumer Product Safety Commission, which protects buyers of goods. It would review contracts for things like mortgages, credit cards and insurance, making sure they're easily understood and modifying or eliminating terms that are dangerous. And it would promote effective, uniform disclosure to make it easier to compare products.

Q. Why do you think it's necessary?

A. Twenty-five years ago, financial products were strictly screened to make sure borrowers could repay and there was no such thing as double-cycle billing or \$49 late fees. Today someone engaging in an ordinary transaction faces an unreadable contract and risks that are nearly impossible to assess. It's like sticking your hand down a dark hole and hoping nothing bites you.

Q. But if I didn't get seduced by a too-good-to-be-true mortgage and I pay my credit card in full, why should I care?

A. Some of what goes on is very sophisticated—you may not even realize you're paying more on your mortgage than you have to. Also, you can say, "Don't be a victim," but it's the government's job to keep predators in check.

Q. Hillary Clinton has put your idea on her agenda. But what happens if a Republican is elected?

A. At some point the demand will be loud enough that politicians will ignore it at their peril. Remember, Nixon was President when the CPSC was created.

Q. Until your idea is a reality, what can we do to protect ourselves?

A. Treat all financial products as dangerous until proved otherwise. Do not carry credit-card debt—none, never, no matter what—because credit-card contracts in particular are loaded with tricks and traps. And because unnecessary debt like that can make your family vulnerable to other bumps in the road. I can't promise that a Financial Product Safety Commission will stop people from overspending on credit cards, but it will help make sure your card isn't misusing you. **\$**



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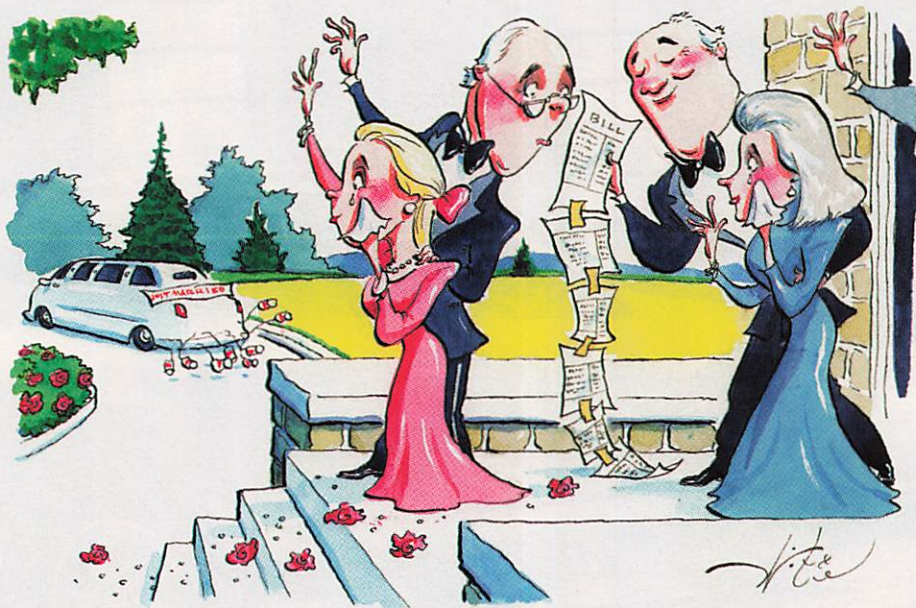
Going Naked on ATM Deposits

You may soon be relieved of the minor hassle of filling out deposit slips and envelopes when you put money into the bank via an ATM. Bank of America, Chase and Wells Fargo have begun rolling out envelope-free ATMs. Just stick your deposit straight into the slot: The machine scans it, reads it, asks you to confirm the amount, and prints a receipt with an image of the check or an inventory of the cash.

WHEN YOU'LL SEE THEM So far only about 4% of U.S. bank ATMs are envelope-free. But the technology should become prevalent over the next five years, says Gil Luria, an analyst at Wedbush Morgan Securities.

WHAT THEY MEAN FOR YOU Money sure looks naked going in. But Luria says you're just as safe depositing checks this way. Your receipt now offers picture proof of the transaction. And the electronic read reduces human error. Your deposits are also available faster (sometimes the same day). One caution: If the ATM messes up—it's rare, experts say—it's your word against the bank's on a cash deposit. So drop bills with a teller. But go ahead, bare your checks. —LAWRENCE LANAHAN

Our Son's In-Laws Are Bilking Us on Wedding Costs! What Do We Do?



Q Before my son got married, my wife and I told his fiancée's parents that, in addition to hosting the rehearsal dinner, we'd pay for one-third of the cost of the wedding (we had a general sense of the overall budget). They were very appreciative and agreed to send us an accounting of expenses post-event. Well, we've received it, and it looks to us as if they padded the bill. What should we do?

Answer Be grateful you didn't offer to pay for half.

Seriously, the first thing to do is everything that discretion allows to determine the actual cost of the event. That means calling all the service providers involved—the caterer, the florist, the band and everyone else—and asking what each of them would charge for a wedding like your son's. In short, nail down the numbers.

Then if they don't add up, say to the bride's parents in your most apologetic voice, "I'm just wondering if there's been some sort of error. We'd been expecting the wedding to cost around [whatever you believe it actually cost]. Could you double-check the math to be certain there's been no mistake?" In other words, without being accusatory, give them a face-saving opportunity to adjust the bill.

And if they don't? While it's perfectly ethical to challenge any bill you believe to be incorrect, you have another obligation here: to support your son's marriage. For the sake of family harmony, hold your nose, write the check and keep your suspicions to yourselves. But never agree to share the cost of anything with these people in the future. \$

? Questions about money and ethics? E-mail our ethicists, authors of *Isn't It Their Turn to Pick Up the Check?* (Free Press), at right_thing@money.com.

...**Recessionary eating** 32% of people are eating out less, 24% are ordering cheaper meals, and 24% are going to less pricey eateries, says NPD...

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Want to Be Rich? Don't Get Too Happy

New research shows income rises with happiness, but bliss can be bad for the bank account

Checked out the bestseller lists

lately? In February you would have spotted motivational expert Marci Shimoff's *Happy for No Reason*, which claims to teach you "how to experience sustained happiness for the rest of your life." In March came *The Geography of Bliss* by journalist Eric Weiner, a travelogue of places on Earth where people are the happiest. Both of these follow on the heels of *Stumbling on Happiness* by Harvard psychologist Dan Gilbert, which has been translated into 20 languages.

Clearly, for a lot of people, finding happiness is the ultimate goal. But should it be? New research suggests maybe not—at least if wealth and success are also at the top of your list.

University of Illinois psychology professor Ed Diener and others have established that while money won't buy happiness, happy people tend to earn more than sad people. A few years ago, however, investing legend John Templeton wrote Diener a letter that had the professor scratching his head. "Is life satisfaction always great?" Templeton asked. "Maybe a little bit of dissatisfaction is okay."

"I started wondering," Diener recalls, "do you have to be happier and happier? How happy is happy enough?"

Thus, a new study was born. Diener

and his colleagues used data from the World Values Survey, which measures the happiness of respondents on a scale of 1 to 10 (with 10 the happiest). They found that income did indeed increase along with happiness but not at the very top. The 10s earned significantly less than the 8s and the 9s. The latter were also more likely to have gone to college, have engaged in the political process and have saved money.

DON'T WORRY, SPEND MONEY

Why is it better to be happy but not euphoric? Diener's take is that happy—but not too happy—people are strivers. They're interested in making the sorts of changes necessary to get ahead in life, including engaging in competition (not always a happy pursuit), obtaining more education and changing their behavior when what they're doing now isn't working. The 10s, on the other hand, are too complacent to adjust enough.

Diener isn't the only dog on this trail. When Duke University finance scholars undertook an examination of optimists using the Federal Reserve's Survey of Consumer Finances, they also found that people who saw the glass as filled to the brim (classified as those who overestimated their own life spans by 20 years or



more) behaved in ways that weren't good for their future.

"When you compare moderate optimists with extreme ones, one of the biggest areas of difference is in self-control," says David Robinson, a lead researcher on the Duke study. The extreme optimists overspent. They accumulated debt. They didn't save. They were more likely to be day-traders. On the other hand, moderate optimists, recognizing the possibility of a run of bad luck, saved more than extreme optimists did.

The idea that you can be too happy applies in other areas of life besides finance. Academic success, for example, went up as happiness increased, Diener found. But it peaked at people classified as "happy" and then fell back for the "very happy."

There are some circumstances in which the very happy have an edge. They're more likely to be successful as volunteers, and they're better at dating and at maintaining close friendships. All keys to life

UPBEAT vs. EUPHORIC

MODERATE OPTIMISTS
Have more wealth

Save more

Work harder

EXTREME OPTIMISTS
Overspend

Day-trade more

Have higher debts



SOURCE: Manju Puri and David T. Robinson.

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QUIZ

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- 4 = Strongly agree
- 3 = Agree
- 2 = Neutral
- 1 = Disagree
- 0 = Strongly disagree



1. In uncertain times, I would expect the best
2. It's easy for me to relax
3. If something can go wrong with me, it will
4. I am always optimistic about my future
5. I enjoy my friends a lot
6. It's important for me to keep busy
7. I hardly ever expect things to go my way.
8. I don't get upset too easily
9. I rarely count on good things happening to me.
10. Overall, I expect more good things to happen to me than bad

Scoring: Only questions 1, 3, 4, 7, 9 and 10 are scored (the others are designed to throw you off). Score 3, 7 and 9 in reverse: 0=4; 1=3; 2 stays the same. A score above 12 (out of 24) means you tend toward optimism. Great. Extreme optimism, though, can hurt you in the wallet.

SOURCE: M.F. Scheier and C.S. Carver.

satisfaction, but not necessarily wealth boosters. Eventually the boss notices that his cherished staffers spend all their time socializing rather than getting work done.

So what are the takeaways from this research? To be sure, it's better to be generally happy than sad when it comes to your finances. But sheer bliss isn't all it's cracked up to be. To keep yourself a bit more balanced, try these two courses of action.

> Surround yourself with the right people.

Take the optimism test above. If you scored at the top or bottom, maybe you need to find a few new friends. "If you're looking to get happier, hang out with the optimists and avoid pessimists," says Frederick G. Crane, executive professor of entrepreneurship and innovation at Northeastern University. If you're too happy, pessimists are the order of the day for you.

> Challenge yourself. Even if you're not constantly floating on a cloud, super-happiness can make you complacent, says Diener. As long as your approach to life and its tribulations is working, after all, why should you try anything new? The problem with such thinking is that when your way of doing things falls short, you may not realize it. The solution: Alter your typical tack to problem solving. In my case, for years the only way I knew to get more work done was to put in longer hours. I had to learn to delegate. Once I did, I gained others' perspective, not to mention my own time. So push yourself in a new direction. You'll be richer for it. \$

Editor-at-large Jean Chatzky appears regularly on NBC's Today. You can contact her at money_life@moneyemail.com.

REPORTING BY ARIELLE MCGOWEN

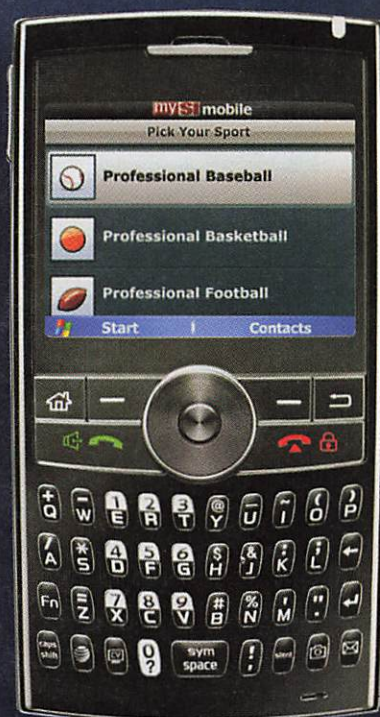
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8 of the "best mutual funds you can buy." — MONEY® magazine, 2/08

Eight T. Rowe Price funds were recently included on MONEY magazine's list of 70 "best mutual funds."* The funds were chosen based on low cost, a history of putting investors' interests first, experienced managers, and a consistent investment strategy.

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*Source: MONEY magazine. The funds on the MONEY 70® were carefully selected using the collective experience and knowledge of the staff of MONEY magazine. Some of the criteria included consistent investment strategy, low expenses, experienced managers, and a strong record of putting shareholder interests first. The ending date for performance was 12/31/07. The publication date of the MONEY article was 2/08. MONEY and MONEY 70 are registered trademarks of Time Inc. Used with permission. **The funds invest in many underlying funds and are exposed to the risks of different areas of the market.

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FAMILY

Are You Ready to Manage Mom and Dad's Money?



Even if you think you're well prepared—*especially if*—you'd better read this **BY WALECIA KONRAD**

EVER SINCE YVETTE MESQUITA took over her father's finances, she's felt as if she's had two jobs. Two years ago, Bill Mesquita's longtime companion died. Overcome with grief, he wasn't able to keep up with day-to-day tasks like bill paying. Before Yvette and her two sisters realized what was happening, their dad had racked up \$30,000 in credit-card debt. »



Mesquita, a 43-year-old parks employee in Tolleson, Ariz., lives about 90 minutes from her now 71-year-old father, so the bulk of the financial management fell to her. She convinced her dad to cut up his credit cards and refinance his mortgage. Then she took over the bills and budgeting so she could make sure that he kept his expenses within the \$40,000 or so he earns from Social Security and a pension. Her quick action helped avert a disaster. But the process hasn't been easy. "The red tape can get overwhelming," she says.

When Mesquita tried to open a joint bank account with her father, for example, she figured the durable power of attorney he'd signed would be sufficient. It wasn't. The bank had its own forms that both she and her dad had to fill out before Mesquita could act on his behalf. Her dad was able to come into the bank to do the paperwork, but the incident worried Mesquita. "I thought I had everything taken care of," she recalls. "What if my dad had been in the hospital? I'm wondering what else the power of attorney won't work for."

More than 34 million people help care for a parent or elderly friend or relative, according to the AARP Public Policy Institute. Whether it's paying the monthly bills, appealing a denied insurance claim

or overseeing an investment portfolio, money management is often the first role adult children take on when they begin assisting an aging parent. Yet few families are adequately prepared.

Without advance planning, just finding files can be a massive undertaking. Often by the time you realize you need to intervene, memory loss or illness are a problem. Your parent may have misplaced statements, forgotten about accounts or, worse, let payments lapse. Even in the best of circumstances, glitches like an insufficient power of attorney are common.

To avoid adding logistical headaches to what's already a fraught transition for both parents and children, every family should follow these five steps long before help is needed.

CREATE A SINGLE GUIDE When you take over another person's finances, you quickly find that you need information and lots of it. That's why everyone, regardless of age or health, should compile a list of financial accounts and documents in case emergency strikes. The list, including

10

Forms you might need to manage a parent's money

SOURCE: MONEY estimates.

account and policy numbers and the location of backup documents, should cover:

➤ **Monthly bills**, including phone, gas, electric and credit-card accounts

➤ **Bank accounts** and safe-deposit boxes

➤ **Retirement accounts**, including Social Security, pensions, IRAs and 401(k)s

➤ **Brokerage and fund accounts**

➤ **Insurance policies**, including life, health, home, auto, long-term care, Medicare B, Medicare D and Medigap

➤ **Wills and medical directives**, including living wills and health-care proxies

Also be sure to note the names of any bank employees, insurance agents, brokers, investment advisers and attorneys.

If you're working with your parents to draft this list, expect to take some time with this task, especially if your parents are disorganized or uncomfortable with the process. You'll also need to make copies of the supporting paperwork. For more help, use the extensive checklist published in *The Parent Care Solution* by Dan Taylor, a book that offers plenty of good advice on how to talk to your parents about money.

Once you've assembled this list, keep the paperwork in an accessible place such as a

3 fast fixes

HOW TO HANDLE THE HARD QUESTIONS

NOW THAT YVETTE MESQUITA and her sisters have their father's finances in order, they need to address an even tougher issue, says planner and elder-care expert Rosanne Grande.

1

Talk about health care.

Even though Dad is doing well, he needs to sign a health-care proxy, which will name someone to make treatment decisions for him, and a living will, outlining his wishes for life-sustaining care. "We've approached Dad several times about this," says Mesquita, "but every time we do, he balks. It's so overwhelming."

2

Bring in help.

Arrange a family meeting, but not at Dad's house, where he's bound to feel defensive. Instead, have an objective outsider—an attorney, a financial planner or an elder-care counselor—lead the meeting. "I've seen older people open up immediately to a professional in ways they never would with their kids," says Grande.

3

Be an example.

One of the best ways to convince a parent to do this paperwork, says Virginia Morris, author of *How to Care for Aging Parents*, is to do it for yourself. After all, everyone needs a living will and health proxy. Then tell your parents how it went. "You get the ball rolling in a nonthreatening way," says Morris.



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SHIFT_durability

MY09 model shown, available August 2008. *Available feature. Always wear your seat belt, and please don't drink and drive. ©2008 Nissan North America, Inc.

home file cabinet. Avoid a safe-deposit box in your parents' names; even if you have permission to open it, the bank may not let you do so without a parent present.

GET THE POWER The next step is making sure you can get control of your parents' accounts if and when you need to step in. If your parents haven't done so already, they each need to draw up a durable power of attorney, which authorizes someone else to take care of personal and financial affairs. The durable part means that the authorization lasts even after the person signing the document becomes incapacitated. A power of attorney with the broadest parameters—the authority to handle all financial, real estate and legal matters—is best, advises Liza Weiman Hanks, an estate attorney and author of *The Busy Family's Guide to Estate Planning*.

If your parent becomes incapacitated without this document, explains Hanks, you'll have to go to court to be named as legal guardian for your mom or dad (a long, costly and potentially humiliating process).

CLOSE THE LOOPHOLES As Yvette Mesquita found out the hard way, a durable power of attorney is not one size fits all. Most large financial institutions require their own forms to be filled out and signed by an account holder before they allow anyone else to access the money. The extra layer is designed to protect your parents from fraud and protect the institution from liability. When you get a durable power of attorney, call each of your financial institutions and ask if the firm requires a supplement.

TAKE SPECIAL CARE WITH HEALTH CARE

If your parents are in good health, you may not realize how important insurance and other medical paperwork is. "This is one of the areas adult children often overlook," says Rosanne Grande, a financial planner with Rogé & Co. in Bohemia, N.Y. and an elder-care expert. "But it's also one of the most problematic areas when things go wrong."

Grande isn't talking just about living wills and health-care proxies, which spell out your final wishes and authorize some-

one to make treatment decisions on your behalf. While these are vitally important documents—for you and your parents—it's also critical to make sure that you can get information on your parents' medical condition and health insurance coverage.

For that to happen, follow these steps. First, if your parents have private insurance, contact the carrier and ask how to become a patient advocate. This will give you the power to handle claims appeals, lapsed coverage and other glitches. You will also be able to receive bills and pay your parents' premiums. With most insurers, says Grande, your parents will have to draft a letter of authorization stating they want you to be their patient advocate. In turn, the insurer will usually send a form that both of you will need to fill out.

Second, you need permission to talk to your parents' medical providers. The reason? With Medicare, only the patient has access to insurance information. To make sure you stay in the loop, have your parents draft a letter of authorization and fill out special forms for each of their doctors. That way, if there is a dispute over a payment or a question over treatment, you can call the provider directly.

GO SLOWLY Once you've built a strong foundation with the right paperwork, it's best to move slowly when it comes to taking over anyone's finances. It's natural for parents to resist, says Virginia Morris, author of *How to Care for Aging Parents*. They're proud of their financial accomplishments and enjoy the independence.

You might start by simply helping your parents write checks for their monthly expenses. With a little time, you may convince them to let you set up automatic bill payments so they don't have to worry about due dates. Ultimately, your parents may decide it's fine for you to receive the bills and take care of paying them directly. Easing the transition gently will build trust and show your parents that you only want to help make life easier, not take away their independence.

"It's a very emotional process," confirms Yvette Mesquita. "Parents take the whole thing very personally, and it's a lot of work for the kids. It takes time." \$



Question of the Month

At What Age Can I Get at My IRA?

Q. I've heard that you can start withdrawing from your IRA without penalty the year you turn 59 1/2, not the month. Is that true?
—Kathy Morgan, Lake Mills, Wis.

A. In most cases you can't make penalty-free withdrawals from a traditional IRA until the very day you turn 59 1/2. The same goes for earnings from your Roth. Take money out before then and the IRS will slap you with a 10% penalty (exceptions include college costs).

You can sidestep the 10% penalty by making extended regular withdrawals, also known as 72(t) withdrawals, beginning at any age. But the IRS enforces the 72(t) rules strictly, warns Howard Hook, a C.P.A. and planner in Roseland, N.J. You generally must use an IRS-approved withdrawal formula for five years or until you reach age 59 1/2—whichever takes longer.

If you don't need your IRA funds at 59 1/2, you will have to contend with a trickier rule 11 years later: You must start taking withdrawals from a traditional IRA no later than April 1 of the year following the year you reach age 70 1/2.

—JANICE REVELL

Meet W1zardF1ngers. Gamer. Hacker. Boy wonder of the underworld. He had it all. But his cyber joyride came to a sudden end. Pwned like a n00b in a first-person-shooter, it was game over.

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70 million people switched to AVG 8.0 because it protects from online threats without slowing PC's or networks to a crawl. That put a lot of hackers, and their threats, out of business. But we're dedicated to the rehabilitation of every lost soul defeated by our award winning software. To help us help them, visit hugsforhackers.org. Do it now, because somewhere there's a hacker who needs a hug.





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walk with someone you trust.

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Out with the Old Stuff

Stringless guitars, Barbie dolls, suits with big shoulder pads, computers that date from the Montreal Olympics—you'd love to rid yourself of the junk, uh, cherished belongings you've amassed. It's not easy. Even the most desperate charity won't take a 20-year-old TV set. If you plan to lighten up but don't think Sotheby's will auction your castoffs, consider these options. —BARBARA BEDWAY

SELLING IT

TO MAKE A LITTLE MONEY

> THE NICE STUFF

Consignment shops accept a wide variety of goods that homes tend to overflow with, including clothing, toys, sporting goods and furniture. Many, though, are choosy. A store may specialize in a specific category or require that clothes be less than three years old and recently dry-cleaned. Typically, you get 40% to 60% of the sales price. If your stuff doesn't sell after a set period, usually 30 to 90 days, you get it back or it's donated.



> THE ODD ITEMS

Auction sites such as eBay allow you to sell items that appeal only to a passionate few, say, that Danish modern yellow gumball lamp.



> HEAVY METAL

Know that broken toaster in your attic and the old fridge in the garage? A scrap-metal dealer might buy them (look in the Yellow Pages under "Scrap Metal"). You're paid by the pound. If you have iron or stainless-steel items, make sure your dealer will accept them; some don't. Aluminum pots will fetch 60¢ to 90¢ a pound, and stainless steel \$1 a pound.



GIVING IT AWAY

YOU'LL HAVE GOOD FEELINGS

> WORKING BUT UNWANTED

Connect with people in your area who are on the prowl for free stuff at freecycle.org. After you find the online group nearest you and sign up, you'll receive listings of stuff people want (or want to get rid of). Recent offers in Nyack, N.Y. included a 20-gallon aquarium, four Hula Hoops, desktop computers and a patio dining set. Also, at craigslist.org you can list free goods for pickup.



> ON ITS LAST GASP

Goodwill (goodwill.org) and the Salvation Army (salvationarmyusa.org) will take just about anything and provide you with a receipt for your goods and not-so-goods so that your donation is deductible. Make sure you list each item you gave as well as its value.



> ELECTRONICS OF YESTERYEAR

You can find out where to recycle your old computers, peripherals, TVs and cell phones at the website of the Electronic Industries Alliance (eia.org). For further recycling options, try manufacturers like Apple and Dell or large retailers such as Best Buy, Office Depot and Staples.



DUMPING IT

SOMETIMES NOBODY WANTS IT

> TRUE JUNK

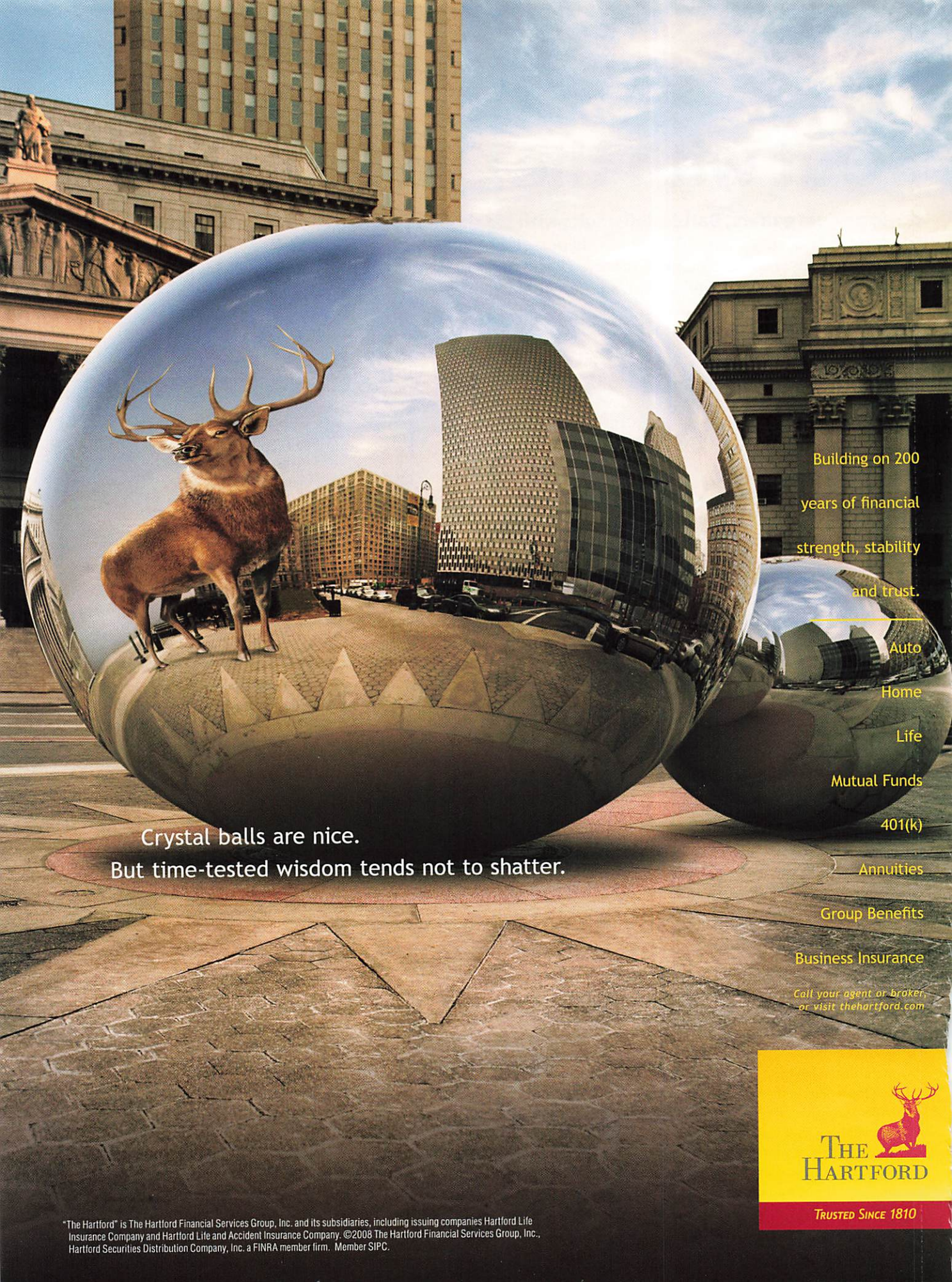
Call 800-GOT-JUNK to have uniformed drivers take it all away—for a price. The fee is based on volume (plus any special recycling surcharges that local authorities add on). Prices for a truckload (15 cubic yards) vary by region; the company's website shows you how much stuff can fit in a truck. The minimum charge ranges from about \$90 to \$110; the maximum, about \$495 to \$695. Another possibility: Check the local Yellow Pages or run "junk removal" and the name of your town through Google for local haulers. You can also ask for a recommendation at your own town dump.



> MIXED MESSES

So-called downsizing specialists help make the hard decisions (whether to sell, donate or dump) for fees ranging from \$50 to \$150 an hour. To find a specialist, try the National Association of Professional Organizers (napo.net) or the National Association of Senior Move Managers (nasmm.com), which caters to the relocation needs of those age 55 and older. \$





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A Rough Landing for Airline Cards

What today's mergers and bankruptcies mean to your mileage credit card

Attention passengers: With the pending Delta-Northwest merger and a potential Continental-United one, be prepared for turbulence in your pocketbook. Typically, when airlines merge, one mileage credit card keeps the awards program. (The other may switch to nonflight rewards; that's what happened to Aloha Airlines'

card after the carrier's spring shutdown.) While you probably won't lose miles, you'll have to stick with the victor to rack up points with the new airline. With the Delta-Northwest merger, U.S. Bank (WorldPerks Visa) and American Express (SkyMiles) will duke it out. A Continental-United merger likely won't be as disrupt-

tive, says Bill Hardekopf of LowCards.com, since Chase issues both cards.

Read your mail closely for updates to your terms, such as point calculations and annual fees. Better yet, consider an option that lets you earn points good on any airline, such as the **Citi PremierPass card** (citicards.com). —ISMAT SARAH MANGLA

SAVINGS

	YIELD	MIN. INVEST.	TELEPHONE
Bank Money-Market Accounts			
AVERAGE	0.64%		
Interwest National Bank (New York)	3.60	\$1,000	212-218-8383
OneUnited Bank (California)	3.60	1,000	877-663-8648
California First National Bank (California)	3.60	5,000	800-735-2465
UFBDirect.com (California)	3.35	1	888-580-0049
IGObanking.com (New York)	3.28	1	888-432-5890
Taxable Money-Market Funds			
AVERAGE	2.23		
Morgan Stanley Active Assets MT	3.07	5,000	800-869-6397
Touchstone Money Market Fund A'	2.97	1,000	800-543-0407
Dreyfus Liquid Assets'	2.92	2,500	800-782-6620
AARP Money Market Fund'	2.90	100	800-958-6457
Fidelity Cash Reserves	2.85	2,500	800-343-3548
Tax-Exempt Money-Market Funds			
AVERAGE	1.78		
Alpine Municipal Money Market Fund Inv.'	2.32	2,500	888-785-5578
USAA Tax Exempt Money Market Fund	2.13	3,000	800-531-8181
American Century T/F Money Market Fund	2.06	5,000	800-345-2021
Vanguard Tax-Exempt Money Market	2.00	3,000	800-851-4999
Marshall Tax-Free Money Market Fund Y'	1.96	1,000	800-236-3863
Taxable Short-Term Bond Funds			
AVERAGE	3.77		
Metro West Low Duration Bond M	5.11	5,000	800-241-4671
USAA Short-Term Bond	5.09	3,000	800-531-8181
Homestead Short-Term Bond Fund	4.91	500	800-258-3030
Morgan Stanley Limited Duration	4.73	1,000	800-869-6397
DWS Short Duration Fund S	4.32	2,500	800-728-3337
Tax-Exempt Short-Term Bond Funds			
AVERAGE	3.36		
Alpine Ultra Short Tax Optimized Income Fund	4.64	2,500	888-785-5578
Wells Fargo Adv. Ult. S/T Muni Inc. Inv.	4.47	2,500	800-222-8222
Wells Fargo Adv. Short Term Muni Bond Inv.	4.05	2,500	800-222-8222
USAA Tax Exempt Short-Term	3.89	3,000	800-531-8181
Pimco Short Duration Muni Income D	3.64	5,000	800-426-0107

	YIELD	MIN. INVEST.	TELEPHONE
Six-Month CDs			
AVERAGE	1.84%		
Corus Bank (Illinois)	3.65	\$10,000	800-989-5101
GMAC Bank (Pennsylvania)	3.60	500	866-246-2265
Nexity Bank (Alabama)	3.41	1,000	877-738-6391
Imperial Capital Bank (California)	3.35	2,000	866-413-5626
One-Year CDs			
AVERAGE	1.92		
Countrywide Bank (California)	4.05	10,000	800-479-4221
GMAC Bank (Pennsylvania)	3.90	500	866-846-2265
Transportation Alliance Bank (Utah)	3.61	1,000	800-837-4136
Advanta Bank Corp. (Utah)	3.60	10,000	800-788-2632
Five-Year CDs			
AVERAGE	2.75		
Capital One (Virginia)	4.50	5,000	866-369-2737
Discover Bank (Delaware)	4.18	2,500	800-347-7000
Transportation Alliance Bank (Utah)	4.17	1,000	800-837-4136
GMAC Bank (Pennsylvania)	4.15	500	866-846-2265

CREDIT

	RATE	ANNUAL FEE	TELEPHONE
Cards with the Lowest Rates			
Pulaski Bank & Trust (Arkansas)*	8.00%	\$0	800-980-2265
Amalgamated Bank of Chicago (Illinois)	8.50	45	800-723-0303
Heartland Bank (Missouri)	10.24	0	800-489-2660
No-Fee Cards with the Lowest Rates			
Pulaski Bank & Trust (Arkansas)*	8.00	0	800-980-2265
Heartland Bank (Missouri)	10.24	0	800-489-2660
Simmons First National Bank (Arkansas)	10.25	0	800-636-5151
Premium Cards with the Lowest Rates³			
Wells Fargo Bank (California)	6.00	19	800-642-4720
Pulaski Bank & Trust (Arkansas)*	6.50	35	800-980-2265
Simmons First National Bank (Arkansas)*,2	7.25	0	800-636-5151
AVERAGE ALL CARDS	11.95		

SAVINGS NOTES AND SOURCES: CD and money-market account data as of April 15 from 100 Highest Yields, a publication of Bankrate.com (\$12.4 for 52 issues; 800-327-7717, ext. 11410); all have a minimum investment of \$10,000 or less. Average tax-exempt and taxable money-market fund yields for the week ended April 17 from Money Fund Report (moneyfundreport.com); all have a minimum investment of \$10,000 or less and assets of \$25 million or more. Average bond fund yields for the month ended March 31 from Lipper; all are medium- and high-quality funds without sales loads and with average maturities of three years or less. *Manager absorbed all or some operating expenses. **CREDIT NOTES AND SOURCES:** All rates subject to change. Credit-card rates are for standard cards as of April 17 from Bankrate.com and are variable unless otherwise indicated. Survey does not include Internet-only cards. *Fixed rate. *Visa only. *Platinum and gold cards.

Mental Health, Fast and Cheap

A low-cost treatment may be able to cure what ails your psyche BY PATRICIA B. GRAY

What if you could get out from under what's been bothering you—anxiety, depression, low self-esteem—in three or four months for about \$320? That's the promise of cognitive behavioral therapy (also called cognitive therapy or CT). It's an intense, short-term treatment that helps you recognize and change harmful thoughts and behaviors. Peter G., 62, a former San Francisco broker and a 30-year veteran of conventional therapy, says it “worked in a very dramatic fashion” for him. “I changed my life within a couple of months. I'd been dealing with depression, panic attacks, issues of abandonment. CT helped me put that all in the past.”

Beloved by insurance companies for its low cost and by patients for its fast results, CT is coming on like gangbusters. Some 50% of psychiatrists now use it in their practice, according to a 2006 study. They, as well as psychologists and social workers, believe it is effective in treating a broad array of conditions, including depression, anxiety, phobias, obsessions, compulsions and even addictions. Unlike with conventional talk therapy, in which patients may get treatment for years, cognitive therapy's adherents claim that in most cases it can provide relief in about 16 sessions. “CBT isn't open-ended,” says Aldo R. Pucci, president of the National Association of Cognitive-Behavioral Therapists. “We expect you to graduate from therapy, and we hope never to see you again.”

› WHY SHORTER IS CHEAPER You'll pay about the same rate

for cognitive therapy as for traditional therapy—\$50 to \$185 an hour. But most employer health plans limit you to 32 visits a year, and many have

A YEAR IN TREATMENT

Cognitive therapy takes around 16 visits at \$100 each. Insurance typically pays 80%. Conventional therapy, which may take years, costs the same, but insurance pays for only 32 visits. You're on the hook for the rest. Co-pays for monthly drug prescriptions may run \$40 each.

TREATMENT TYPE	ANNUAL OUT-OF-POCKET
› Conventional talk	\$2,640
› Drugs	\$480
› Cognitive behavioral therapy	\$320

SOURCES: 2007 Mercer/Marsh Survey on Health, Productivity and Absence Management; MONEY research.

you pay higher deductibles and co-pays for mental-health treatment than you would for ordinary medical care. Because CT takes only about 16 sessions, you're likely to be reimbursed for most of the costs under almost any health

plan. If your insurer pays 80% of each \$100 visit, your total outlay would be only \$320.

CT can also be less expensive than drug therapy, which three out of four adults prefer for their mental maladies, says David Whitehouse, M.D., a medical director of OptumHealth Behavioral Solutions, a unit of United

found that CT's quickie approach can be as effective as medication for certain conditions. The *American Journal of Psychiatry* recently published a study of people with mild to moderate depression whose symptoms were alleviated after cognitive therapy; MRI scans of their brains showed changes in the two regions associated with depression. Another study found CT to be much more effective than a drug commonly used to treat insomnia in older adults.

› WHAT TO EXPECT ON THE COUCH No more waxing on about childhood traumas on a psychiatrist's divan. Cognitive therapy requires your active participation. Your therapist gives you the tools to overcome negative or irrational thoughts, including relaxation and breathing exercises that help allay anxieties and fears. Ultimately, you learn to be your own therapist. Says Peter G.: “When I find myself awake and ruminating over some problem at 2 a.m., I grab a sheet of paper, analyze my troubling thoughts and come to the conclusion that every-





I have poor leg circulation.

And I have a good reason to try to reduce the risk of heart attack or stroke that comes with it.

Plavix can help

Peripheral Artery Disease (P.A.D.) is often described as poor leg circulation, which puts you at double the risk of heart attack or stroke. That's because, if you have poor blood circulation in your legs, you may also have it in your heart and brain. You may feel nothing, but the most common symptom of P.A.D. is pain or heaviness in the legs.

Take the next step. So if you're diagnosed with P.A.D., ask your doctor about a treatment clinically

To learn more, talk to your doctor today or visit www.plavix.com/PAD or call 1-800-459-7391.

IMPORTANT INFORMATION: If you have a stomach ulcer or other condition that causes bleeding, you should not use PLAVIX. When taking PLAVIX alone or with some other medicines including aspirin, the risk of bleeding may increase so tell your doctor before planning surgery. And, always talk to your doctor before taking aspirin or other medicines with PLAVIX, especially if you've had a stroke. If you develop fever, unexplained weakness or confusion, tell your doctor promptly as these may be signs of a rare but potentially life-threatening condition called TTP, which has been reported rarely, sometimes in less than 2 weeks after starting therapy. Other rare but serious side effects may occur.

Please see important product information on following page.

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WITHOUT PLAVIX



WITH PLAVIX



proven to help reduce your risk of heart attack and stroke

associated with P.A.D. PLAVIX helps keep blood platelets from sticking together and forming dangerous clots, the cause of most heart attacks and strokes. Ask your doctor about PLAVIX.

Plavix.
(clopidogrel bisulfate) 75mg tablets

Help reduce your risk of heart attack or stroke.



If you need help paying for prescription medicines, you may be eligible for assistance. Call 1-888-4PPA-NOW (1-888-477-2669), or go to www.pparx.org.

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WHO IS PLAVIX FOR?

PLAVIX is a prescription-only medicine that helps keep blood platelets from sticking together and forming clots.

PLAVIX is for patients who have:

- had a recent heart attack.
- had a recent stroke.
- poor circulation in their legs (Peripheral Artery Disease).

PLAVIX in combination with aspirin is for patients hospitalized with:

- heart-related chest pain (unstable angina).
- heart attack.

Doctors may refer to these conditions as ACS (Acute Coronary Syndrome).

Clots can become dangerous when they form inside your arteries. These clots form when blood platelets stick together, forming a blockage within your arteries, restricting blood flow to your heart or brain, causing a heart attack or stroke.

WHO SHOULD NOT TAKE PLAVIX?

You should NOT take PLAVIX if you:

- are allergic to clopidogrel (the active ingredient in PLAVIX).
- have a stomach ulcer
- have another condition that causes bleeding.
- are pregnant or may become pregnant.
- are breast feeding.

WHAT SHOULD I TELL MY DOCTOR BEFORE TAKING PLAVIX?

Before taking PLAVIX, tell your doctor if you're pregnant or are breast feeding or have any of the following:

- gastrointestinal ulcer
- stomach ulcer(s)
- liver problems
- kidney problems
- a history of bleeding conditions

WHAT IMPORTANT INFORMATION SHOULD I KNOW ABOUT PLAVIX?

TTP: A very serious blood condition called TTP (Thrombotic Thrombocytopenic Purpura) has been rarely reported in people taking PLAVIX. TTP is a potentially life-threatening condition that involves low blood platelet and red blood cell levels, and requires urgent referral to a specialist for prompt treatment once a diagnosis is suspected. Warning signs of TTP may include fever, unexplained confusion or weakness (due to a low blood count, what doctors call anemia). To make an accurate diagnosis, your doctor will need to order blood tests. TTP has been reported rarely, sometimes in less than 2 weeks after starting therapy.

Gastrointestinal Bleeding: There is a potential risk of gastrointestinal (stomach and intestine) bleeding when taking PLAVIX. PLAVIX should be used with caution in patients who have lesions that may bleed (such as ulcers), along with patients who take drugs that cause such lesions.

Bleeding: You may bleed more easily and it may take you longer than usual to stop bleeding when you take PLAVIX alone or in combination with aspirin. Report any unusual bleeding to your doctor.

Geriatrics: When taking aspirin with PLAVIX the risk of serious bleeding increases with age in patients 65 and over.

Stroke Patients: If you have had a recent TIA (also known as a mini-stroke) or stroke taking aspirin with PLAVIX has not been shown to be more effective than taking PLAVIX alone, but taking aspirin with PLAVIX has been shown to increase the risk of bleeding compared to taking PLAVIX alone.

Surgery: Inform doctors and dentists well in advance of any surgery that you are taking PLAVIX so they can help you decide whether or not to discontinue your PLAVIX treatment prior to surgery.

WHAT SHOULD I KNOW ABOUT TAKING OTHER MEDICINES WITH PLAVIX?

You should only take aspirin with PLAVIX when directed to do so by your doctor. Certain other medicines should not be taken with PLAVIX. Be sure to tell your doctor about all of your current medications, especially if you are taking the following:

- aspirin
- nonsteroidal anti-inflammatory drugs (NSAIDs)
- warfarin
- heparin

Be sure to tell your doctor if you are taking PLAVIX before starting any new medication.

WHAT ARE THE COMMON SIDE EFFECTS OF PLAVIX?

The most common side effects of PLAVIX include gastrointestinal events (bleeding, abdominal pain, indigestion, diarrhea, and nausea) and rash. This is not a complete list of side effects associated with PLAVIX. Ask your doctor or pharmacist for a complete list.

HOW SHOULD I TAKE PLAVIX?

Only take PLAVIX exactly as prescribed by your doctor. Do not change your dose or stop taking PLAVIX without talking to your doctor first.

PLAVIX should be taken around the same time every day, and it can be taken with or without food. If you miss a day, do not double up on your medication. Just continue your usual dose. If you have any questions about taking your medications, please consult your doctor.

OVERDOSAGE

As with any prescription medicine, it is possible to overdose on PLAVIX. If you think you may have overdosed, immediately call your doctor or Poison Control Center, or go to the nearest emergency room.

FOR MORE INFORMATION

For more information on PLAVIX, call 1-800-633-1610 or visit www.PLAVIX.com. Neither of these resources, nor the information contained here, can take the place of talking to your doctor. Only your doctor knows the specifics of your condition and how PLAVIX fits into your overall therapy. It is therefore important to maintain an ongoing dialogue with your doctor concerning your condition and your treatment.

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PLA-OCT07-B-Aa

thing isn't perfect in the universe but I can be happy."

Your therapist will likely assign reading between sessions, and you may be required to keep a daily log or map out a plan for handling situations that spark anxieties. "Like learning how to tie your shoe or ride a bike, cognitive therapy is based on practice, practice and more practice," says Michael R. Edelstein, a San Francisco clinical psychologist.

➤ **WHEN FASTER ISN'T BETTER**
CT is no panacea. Many patients won't take the trouble to do homework or prefer the simplicity of drugs. Some mental-health experts believe that severe illnesses such as schizophrenia, chronic, relapsing depression and serious personality disorders require drug treatments to treat. But studies have shown that CT is effective in reducing symptoms of such illnesses.

➤ **HOW TO FIND A THERAPIST**
Check the websites of the Academy of Cognitive Therapy (academyofct.org) and the National Association of Cognitive-Behavioral Therapists (nacbt.org) for CT practitioners in your area. If you can't find one in your health plan, you may want to go outside your network because the CT costs so much less than traditional therapy.

Once you find a therapist, interview him or her over the phone. You can ask how he or she would handle your problem and how long therapy will take. The answer should be between eight and 20 weeks. Edelstein goes so far as to suggest that you ask for a money-back guarantee. Finally, don't be a patient patient. If you don't see some improvement in three or four sessions—and you're doing your homework diligently—find another therapist. \$

Patricia B. Gray is a medical writer and former editor-in-chief of Dartmouth Medical School's Internet venture. E-mail her at health_wealth@money.com.



Tune Out the Global Hype

You should invest internationally, but not because your adviser just fell in love with overseas funds

At the financial adviser conferences I've attended lately, international investing has been the craze. It's what speakers are touting and exhibitors are pitching. And it's easy to see why: Everybody loves a winner.

A few years ago, when I recommended that clients keep a third of their stock investments in foreign shares, the typical response was "I can't go that high—that's too risky." They resisted because of a trait known as familiarity bias; you're more inclined to invest close to home because it seems safer.

But after five years of outrageously good returns in overseas markets—from 2003 through 2007, international stocks rose 168% vs. 82% for U.S. stocks—that resistance is gone. When I make the same recommendation today, most clients say "Why only a third?" Familiarity bias has been beaten back by another trait: a desire to get behind a winner.

As always, you can depend on many financial advisers to take advantage of your change of heart and push the hottest performers of late. After all, it's simple to sell you something you're already inclined to buy. Unfortunately, it's for all the wrong reasons.

If you're loading up on foreign stocks

now, you're buying near the top of the market. And if your adviser is pushing you into international stocks because of how well they've done, you can be sure he's guilty of performance chasing too.

MY ADVICE

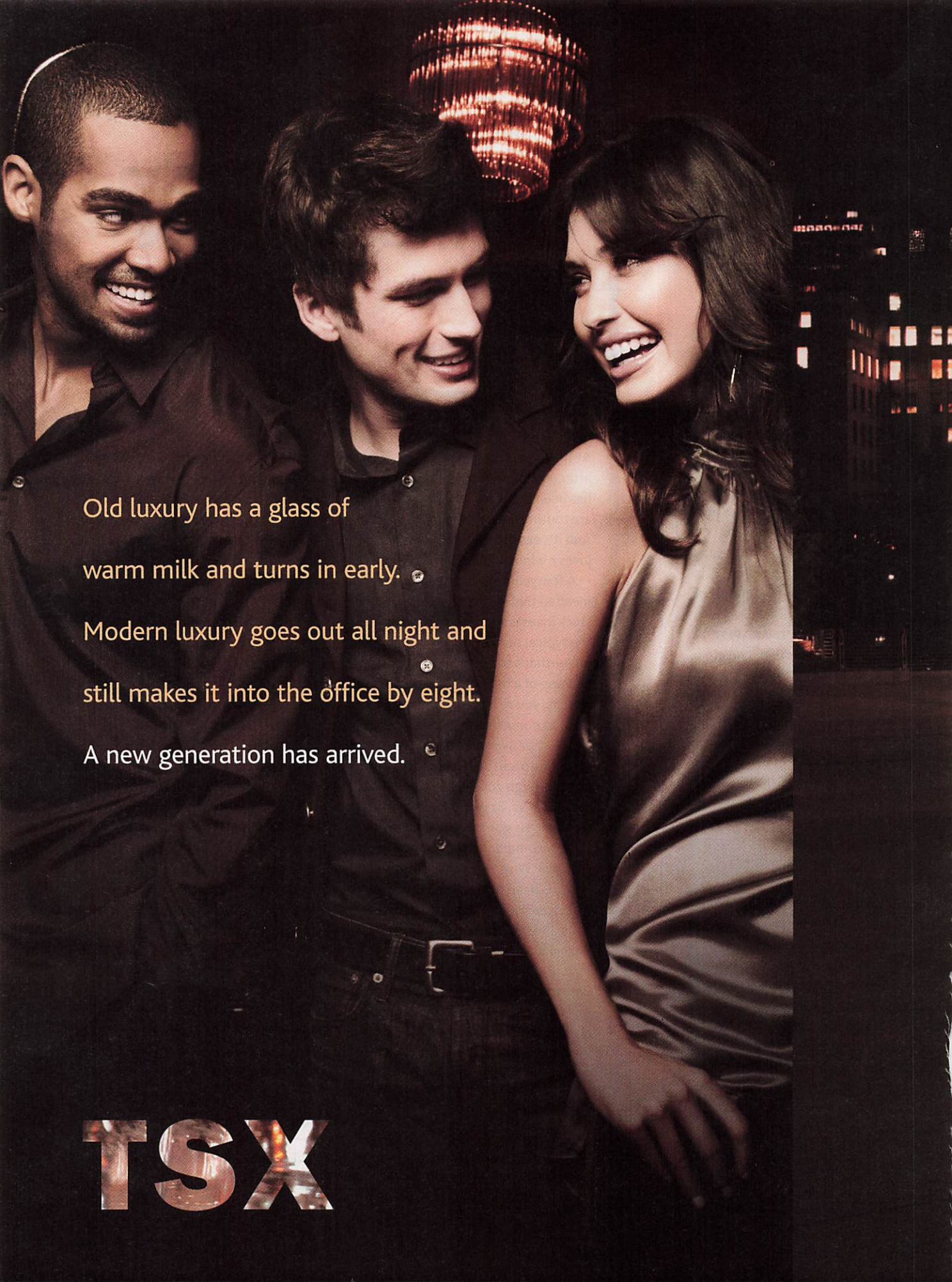
➤ **I still believe you should keep about a third** of your equity portfolio in international stocks, but not because they are hot today. Don't invest overseas because you think your adviser has a clue about which markets are going to do better in the coming years.

Do it because we live in a global economy—international markets make up about 55% of the total value of world markets. You don't get enough foreign exposure by buying U.S. multinationals, as evidenced by the large gap between U.S. and international returns. Still, we are going to spend more of our money in dollars than in euros or yen, so a third seems like a big enough stake to me.

➤ **Here and abroad, expenses matter.** Buy international stocks through a low-cost index fund or an ETF.

➤ **Don't bet on individual countries** or regions. Think of hot investments as being like frying pans: Grab them while they're still hot and you'll get burned.

The Mole is a certified financial planner and certified public accountant who—in the interest of fairness—thinks you should know what goes on behind the scenes in financial planning. Want to make contact? E-mail themole@money.com.



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warm milk and turns in early.

Modern luxury goes out all night and
still makes it into the office by eight.

A new generation has arrived.

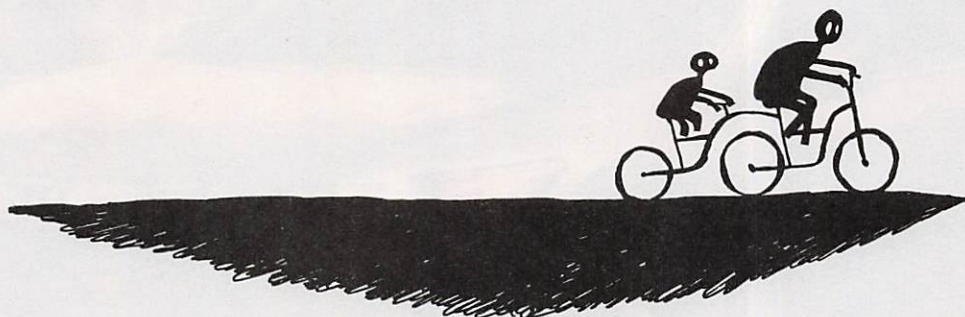
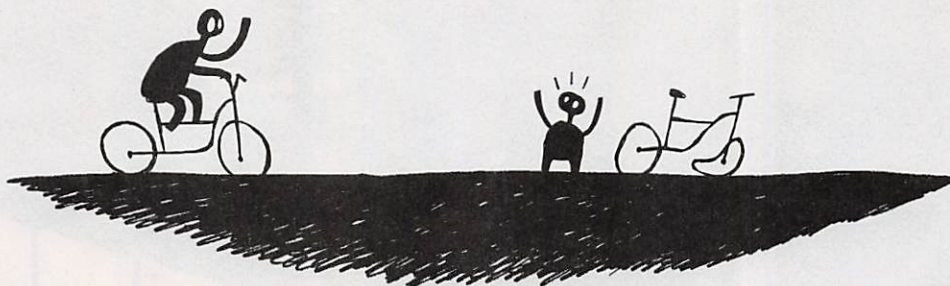
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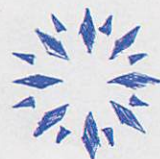




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Reverse Mortgages: Beware the Come-Ons

The loans can help you tap the equity in your house. Just don't get tripped up by greedy salespeople.

► **Last year, borrowers took out** more than 132,000 reverse mortgages—50% more than the year before and almost 10 times as many as five years ago. Such loans, as you may already know, allow you to draw down your home equity if you're 62 or older without repaying it as long as you stay in your house.

That's good news. Reverse mortgages can help cash-strapped retirees generate extra money for living expenses, pay for home improvements, lower other debts or fund the occasional splurge.

There's also a downside to reverse mortgages' growing popularity, however. Loan-origination fees that can top \$7,000 on a \$500,000 home are attracting aggressive salespeople intent on getting you to take out a reverse mortgage whether you need one or not. Some may try to persuade you to invest the proceeds in high-priced financial products, such as annuities, boosting their commissions even more.

No one can say how widespread such tactics are. But the Senate Special Committee on Aging was concerned enough to hold a hearing in December, while FINRA (the Financial Industry Regulatory Authority) issued an investor alert in March. Several lawsuits have also been filed, including a class-action alleging, among other things, that Financial Freedom, one of the largest reverse-mortgage lenders, encouraged brokers to steer seniors into the loans under the guise of providing financial planning services. Financial Freedom says the allegations "are baseless and without merit" and that the company "does not sell, require, promote or recommend annuities to reverse-mortgage borrowers."

So if you've been considering a reverse mortgage, how can you avoid making a misstep? Follow these three tips.

► **Make sure you really need it**

A reverse mortgage can generate cash, but it's not the only way or necessarily the best. Up-front costs can exceed 10% of the loan, making a reverse mortgage a very expensive option if you're borrowing a small amount or you plan to move in a few years. In such cases, you might pay far less by taking out a home-equity line of credit. And hanging on to your home might not be a great idea. You may be able to generate more income by selling and moving to a less expensive place.

► **Look out for the product pitch**

A 2006 AARP survey found that one in 10 reverse-mortgage borrowers had been pitched a financial product along with their loan, most often deferred annuities



but also long-term-care policies. Buying an annuity with reverse-mortgage proceeds rarely makes sense though. As the example below shows, you're unlikely to earn more with an annuity than you are being charged in interest and fees on the reverse mortgage. Worse, you might have to pay surrender charges that are upwards of 20% to take money out in the first few years.

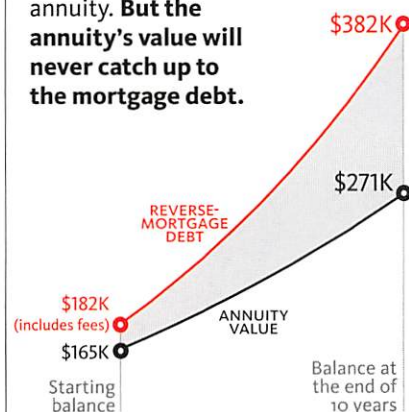
Using a reverse mortgage to pay for long-term-care insurance is tougher to evaluate since it depends on your assets and resources, the cost of the policy and the odds you'll end up in a nursing home for an extended period. "But as a general rule," says Donald Redfoot of AARP's Public Policy Institute, "if you've got to borrow to be able to pay for the cost of a long-term-care policy, then you're probably not a good candidate for one."

► **Get help from a financial planner**

The federal government requires you to meet with a counselor before taking out a reverse mortgage. The quality of the counseling is uneven though. This spring, HUD will promulgate new standards for counseling and require a discussion of the implications of using loan proceeds to buy annuities. If you want a rigorous analysis of whether you're better off with a reverse mortgage or a less expensive home, however, you should consult a fee-only financial planner. (Don't let him sell you an annuity either!) After all, you want to be sure that the equity you took years to accumulate enriches your retirement rather than a salesman's wallet. **\$**

SURE LOSER

A salesperson might prod you to get a reverse mortgage so you can buy an annuity. **But the annuity's value will never catch up to the mortgage debt.**



NOTES: Projected balance for first 10 years. Reverse-mortgage interest rate of 7.3% is for an FHA HECM fixed-rate loan. Rate includes annual mortgage insurance premium but not closing costs. Annuity rate of 5.1% is for a 10-year CD annuity.
SOURCES: Financial Freedom, AnnuityAdvantage.com.

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Think It Possible.SM

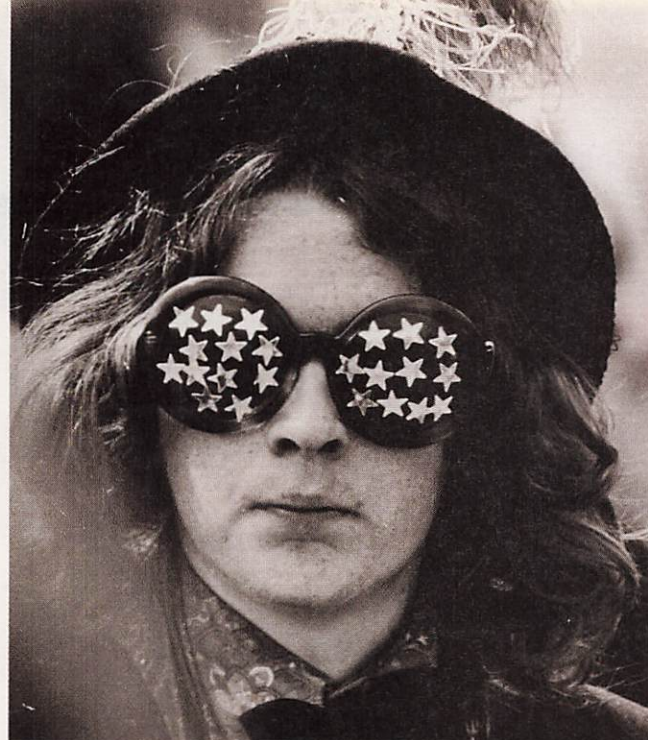


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Baby Boomers: Market Busters?

If you haven't heard, and somehow we suspect you have, the first batch of baby boomers hit Social Security age in 2008. So what happens as this giant generation—78 million strong—quits and starts selling the assets they've saved for retirement? Take our quiz to see. BY DAVID FUTRELLE



Q. The first of the baby boomers were born in 1946, as soldiers back from W.W. II got busy on the domestic front, if you know what we mean. When is the boom considered to have ended?

- a) 1955
- b) 1961
- c) 1964
- d) 1972

A. (c) We're starting off with an easy question. But the point is this: The baby boom stretched over 19 years, and the boomers' retirement will be similarly

stretched out, as will its various financial ramifications. Moreover, the birth rate didn't plummet in 1965; it merely dropped somewhat.

Q. Today, Americans hold \$6.2 trillion in their 401(k)s. In 2040, after the bulk of the boomers have retired and spent considerable portions of their savings, how much are Americans projected to have in 401(k)s?

- a) \$3 trillion
- b) \$9 trillion
- c) \$18 trillion
- d) \$45 trillion

A. (d) That's the projection (in today's dollars) by finance professors James Poterba, Steven Venti and David Wise. Why would the amount in 401(k)s increase so dramatically during the very years boomers retire en masse? Well, because younger people are signing up in greater numbers than their boomer elders did at the same age and investing more. Boomer 401(k) withdrawals should be more than offset by the money that Generations X and Y will put in.

Q. In the Social Security system, current workers finance current benefits. In 1950, there were eight people of working age (15 to 64) for every person 65 and older. Owing to declining fertility rates and our tendency to live longer, now it's 5 to 1. If demographic trends hold, what will the ratio be in 2050?

- a) Half a worker per retiree
- b) Three to one
- c) Five to one
- d) Seven to one

A. (b) Our increasingly skewed "dependency ratio" will put increasing pressure on Social Security and Medicare and likely lead to benefits changes. But some economists point to immigration as a partial fix: While the American population grows older, developing nations are overflowing with young people, many of them well educated and eager to work here.

Q. The richest 10% of boomers own what percentage of the total financial assets held by their generation?

- a) 25%
- b) 47%
- c) 54%
- d) 68%

A. (d) What difference does this make, except to make 90% of us jealous? Here's what: Wealthier people don't need to sell off all their stocks and bonds to retire well, so they tend to hold them, presumably to give to their good-for-nothing offspring. (Some 84% of all older boomers expect to leave their kids a bequest.) This means a lot less downward pressure on stocks when the boomers retire.



Q. What does this chart represent?



- a) Total eclipse of the sun
- b) That scary video from *The Ring*
- c) A hole in one, viewed from inside the hole
- d) Projected share of tax revenue consumed by entitlement spending in 2010, 2040 and 2050

A. All answers are correct, but only the last one should concern you. While total tax revenue is projected to remain more or less constant, at about 19% of total gross domestic product (GDP), spending on Social Security, Medicare and Medicaid is expected to balloon from 8% in 2010 to 18% of GDP by 2050 because of the graying of boomers and the increasing cost of health care. How will the government pay for everything else? Exactly. Expect tax increases, program cuts, deficit spending or a mix of the three.

Q. A typical new house costs you \$244,100 today. How much did an early boomer buying in 1976 pay on average?

- a) \$39,500
- b) \$44,200
- c) \$76,100
- d) \$98,000



A. (b) Nearly eight in 10 boomers own their homes; for most, it's their largest asset outside their pensions. While some worry that a boomer real estate

sell-off may cause an even greater housing crash than today's, data from the Center for Retirement Research at Boston College suggest that these fears may be overblown: Home-ownership rates tend to remain stable until age 80, and decline only moderately thereafter.

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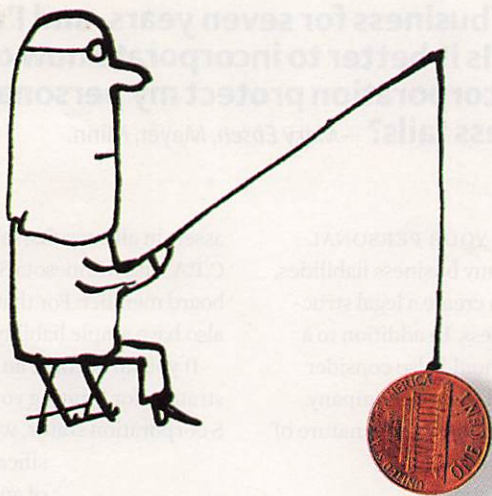


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HOW CAN I FIND CASH TO START A BUSINESS?

Answers to your questions about going solo

Where can I get a small start-up loan for my business? —Mary, Slidell, Miss.

A WHEN IT COMES TO FINDING money to start your business, you have a number of options, from banks to individual investors. But most financing experts suggest looking at your own resources first. Consider borrowing from family and friends or tapping the value in your home through either a home-equity line of credit (HELOC) or a second mortgage.

Once you're up and running and ready for outside assistance, the Small Business Administration (sba.gov) should be your first stop. The SBA doesn't lend to business owners directly; it sets loan guidelines for lenders, community groups and microloan providers and minimizes the risk for lenders by offering guarantees.

While each bank has its own criteria, you can get an idea of what lenders want to see from Bank of America, a top SBA lender. "What we look at is the amount of time the business has been established, the owner's personal credit history and relationship with the bank," says Mark

Hogan, president of small business banking at B of A.

If your start-up company doesn't meet a traditional lender's stringent standards, consider other SBA-supported products, such as microloans or Community Express Loans. These small loans offered by certain lenders can give you a chance to start or expand a business when more traditional sources of money aren't available. Typically, you get a \$25,000 to \$50,000 credit line that you have to pay back in seven to 10 years; rates are variable, generally prime plus 4.25 percentage points. "They are very quick and easy and do not require any collateral or tax returns or business plans," says Sue Malone, founder of Strategies for Small Business, a Community Express Loan provider (strategiesforbusiness.com). "It helps develop credit in the business name and keeps the owners from using their credit cards to start their business, which in this current climate is the kiss of death." For more information, go to sba.gov and click on 7(a) Loan Programs under Services. —ALISON WOO

How can I write a winning business plan with ever-changing financial information?

—Emmanuel, Nairobi

A WRITING A BUSINESS PLAN IS one of the most important—and frustrating—tasks for a small business owner. But stop worrying so much about the numbers. The most crucial aspect of your business plan is you: your skills and experience and your ability to make the case for your business. "The relationship between an entrepreneur and investors is in many ways like a marriage," says Fred E. Wainwright, executive director of the Center for Private Equity and Entrepreneurship at Dartmouth's Tuck School of Business. "Rapport, patience and communication skills are essential."

After management skills, what's most important is market size. To generate interest and inspire confidence, you need to demonstrate that the market for what you do (or make) is large enough to justify the potential of your company—and your business plan should back up your assumptions with surveys, focus groups, customer feedback and industry reports.

Continued on page 56 →



Need help with your business? Your Shop is written by the editors of MONEY's sister publication, Fortune Small Business. Submit your questions to FSB's experts and to other small business owners at cnmoney.com/askfsb.

Finally, says Wainwright, don't try to sell potential investors on numbers you can't possibly predict. Projected financials—your balance sheet and income and cash-flow statements—should be approximated to the nearest thousand. "Nothing makes an investor's eyes glaze over like financial projections five years out that are in dollars and cents," he adds.

Take your time to carefully consider the assumptions behind the projections. "Investors like having the sense that the entrepreneur is committed to underpromising and overdelivering in financial performance rather than attempting to guess or impress with faulty estimates," Wainwright says.

—KATHLEEN RYAN O'CONNOR

A WINNING BUSINESS PLAN SHOULD START WITH A TWO-PAGE EXECUTIVE SUMMARY THAT CONCISELY ADDRESSES THESE 10 TOPICS.

The body of your plan should provide more details and supporting data. Twenty to 30 pages is sufficient; put any excess data in an appendix.

● **MISSION** Be simple and inspiring.

● **PROBLEM AND SOLUTION** Describe your value proposition.

● **MARKET** Clearly define your target.

● **COMPETITORS** Acknowledge the barriers to entry.

● **MANAGEMENT TEAM** Describe relevant experience and advisers.

● **OPERATIONS** Demonstrate that you can grow once business picks up.

● **INVESTMENT NEEDED** Put your request on the table.

● **INTENDED USES OF CASH** Spell out your spending plan in detail.

● **FINANCIAL FORECASTS** Include the assumptions you're making.

● **EXIT STRATEGY** Summarize recent industry examples.

I've been in business for seven years, and I'm a sole proprietor. Is it better to incorporate now or wait? How will incorporation protect my personal assets if my business fails? —Mary Ebsen, Mayer, Minn.

A TO SHIELD YOUR PERSONAL assets from any business liabilities, it's crucial that you create a legal structure for your business. In addition to a corporation, you should also consider becoming a limited-liability company. Which is better depends on the nature of your business, as well as its annual revenue and number of employees.

Forming a corporation is more complicated and costly than forming an LLC. For one thing, you must create a board of directors. By contrast, the administrative requirements for an LLC are relatively simple: You sign an operating agreement, file an annual tax return and keep a separate bank account for your business.

The LLC is often a logical choice for sole proprietors like you. As an LLC you will still be taxed as a sole proprietor, but your business will be a separate legal entity. You can't be held personally liable if your company breaches a contract, for example. However, if you run a personal-service business (such as a day-care center), becoming an LLC may not protect your

assets in all lawsuits, says Carl Peterson, C.P.A. and Minnesota Society of C.P.A.s board member. For that reason, you should also have ample liability insurance.

If you do become an LLC, consider this strategy for limiting your taxes: Apply for S corporation status, which is a tax classification. As the owner of an S corporation, you may designate part of your company's income as wages and part as distributions (which you can withdraw or reinvest in the business). You'll owe payroll taxes of 15.3% of the wages but only ordinary income taxes on the distributions.

Before you try this, keep these two cautions in mind, says Peterson. Taking too little in wages can be an audit red flag with the IRS. Plus, by lowering your wages you'd also be limiting how much you could save in a tax-deferred retirement plan.

The SBA offers free counseling about incorporation through nonprofit partners the Women's Business Centers, SCORE and the Small Business Development Centers. Or consult a tax professional with small business experience. —JULIE FREESE



Online Resources

FOR START-UP CASH

> VirginMoneyUS.com

If you're raising money from friends and family, make it official at this site.

> BusinessFinance.com

Search for a loan or venture-capital money from more than 4,000 funders.

FOR HELP INCORPORATING

> usa.gov/business/incorporate.shtml

Link to your state's official site for incorporating or licensing a business.

> BizFilings.com

Read articles, use the site's state filing service or incorporate in as little as 24 hours with the rush service.

FOR BUSINESS PLANS

> SBA.gov

Visit the Small Business Advisor section to learn about writing a plan.

> BPlans.com

Browse through the site's collection of more than 200 sample business plans.

—HIBAH YOUSUF

WHERE DO MILLIONS OF SMALL BUSINESS OWNERS GO FOR ADVICE?

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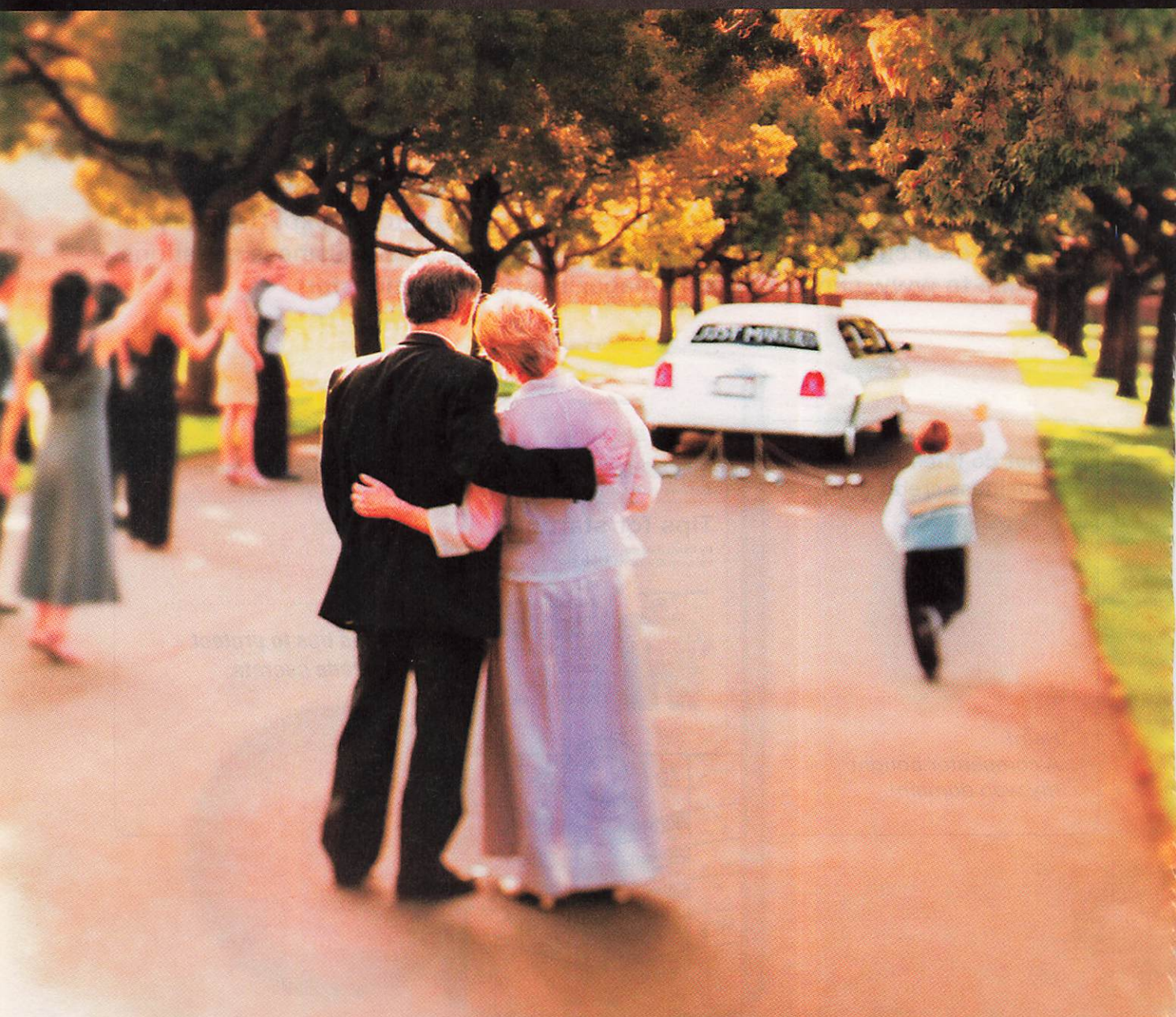
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YOUR PORTFOLIO

How to Thrive in a Barren Market

Stocks have been stranded for a decade. But times like these require the resolve to forge ahead—despite the pain. BY JASON ZWEIG

SOME PUNDITS INSIST THAT we're not in a bear market, since stocks have yet to lose at least 20% of their value. But they're missing the point. Investing in equities in the past decade has been akin to being marooned on a desert island. Yes, you've survived. But the fact remains that your stocks have pretty much gone nowhere for 10 years.

In fact, since the end of March 1998, Standard & Poor's 500 index of blue-chip stocks has returned only 3.5% a year. Even cash has outperformed U.S. equities in this arid market, growing 3.8% annually.

This isn't the first time that stocks have been stranded for such an extended period of time. After the start of the Great Depression in 1929, it took nearly a quarter-century for equity prices to fully recover. >>



Stock prices were also essentially flat between 1966 and 1982. Today's barren market hasn't lasted nearly as long, but it still raises a hard question: What should you be doing to rescue your portfolio?

The short answer is that you need to diversify—but in more ways than you think. You already know the importance of owning different types of assets. Diversification was certainly invaluable over the past 10 years. While U.S. stocks languished, bonds and foreign equities each grew at better than a 7% annual clip. Real estate investment trusts performed even better, returning 10.5% a year.

As a result, a portfolio of some U.S. stocks and foreign equities, bonds and REITs ended up performing well during one of the worst decades for stocks. True, since the market's October peak, traditional diversification hasn't helped much, as several asset classes have fallen at the same time. But as the graphic below shows, diversification works its magic over longer stretches of time.

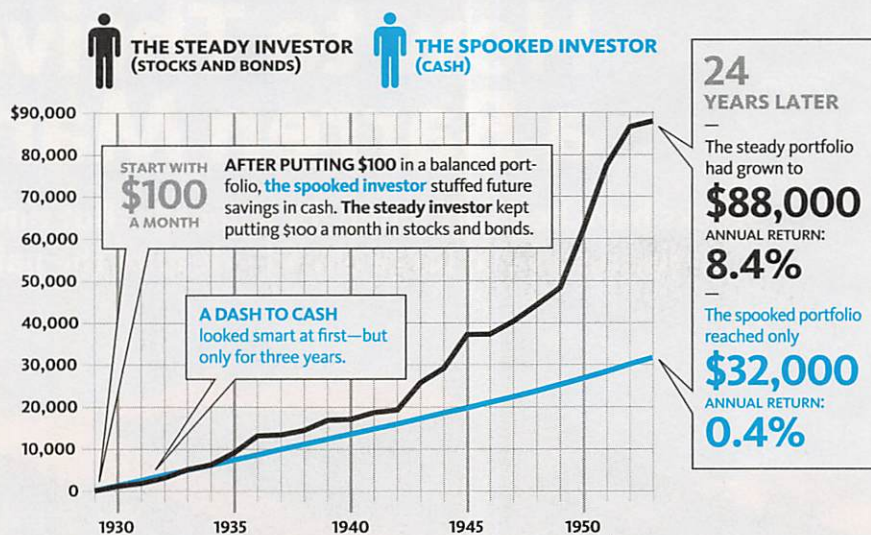
ANOTHER WAY TO DIVERSIFY

Time is precisely the point. In fact, time itself is another great diversifier. In addition to mixing up the types of investments you own, you also need to diversify when you buy them. The thought of investing continuously, in routine intervals, in a go-nowhere market is probably about as appealing as sticking your finger in a light socket. But history says you have to be willing to forge ahead.

Why? For starters, no one can predict in advance which assets will perform best in the future. Stocks? Bonds? Domestic? Foreign? Moreover, bull markets typically begin just when you would least expect

SURVIVOR STRATEGY

Let's compare the fate of two hypothetical investors, both of whom started putting away \$100 a month at one of the worst times—the start of the 24-year stretch from 1929 to 1953, when stock prices essentially went nowhere. The difference: While one got scared and directed future savings into cash, the other continued making monthly investments into stocks and bonds.



them to: in the midst of recessions, says Steve Leuthold of the Leuthold Group.

Therefore, the most sensible approach is to dollar-cost average—in other words, put a fixed amount of money into the market every month or quarter so you're constantly investing at different prices. Check out how this strategy would have performed, hypothetically, during and after the Depression.

Say you had invested in a balanced portfolio consisting of 60% U.S. stocks and 40% intermediate Treasury bonds between the start of September 1929 and August 1953. You would have gained just 6.4% a year,

which is substantially lower than the historical average of 8.8% for this mix. But had you dollar-cost averaged monthly into such a portfolio in that difficult market, you'd have earned a much balmier 8.4% a year.

Dollar-cost averaging was also more fruitful than hiding in cash. Had you begun investing \$100 a month (again, hypothetically) in a balanced portfolio in 1929—and kept investing \$100 a month for the next 24 years—you would have amassed nearly three times as much as an investor who had chickened out and stashed \$100 a month in cash (see the chart above).

Of course, there are no guarantees that investing more money when stocks are down will always deliver better performance in an extended downturn. But at the very least, it will ensure that you benefit from the eventual recovery. So if you don't yet have an automatic investment plan that painlessly transfers a small amount every month from your bank account to a mutual fund, set one up now. Just call your bank or fund company to get the ball rolling.

Doing this probably won't make you

THE TRIUMPH OF DIVERSIFICATION

Though some investors are questioning the value of diversification, owning a mix of bonds and stocks—and different types of stocks—has worked out well over the past decade.

3.5%
S&P 500

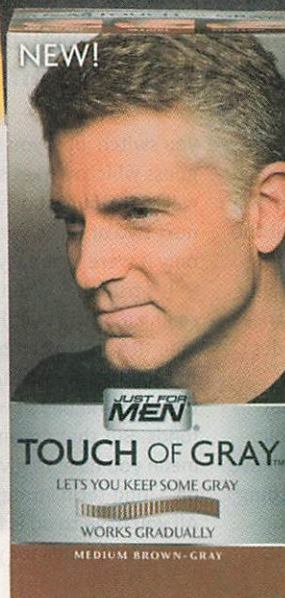
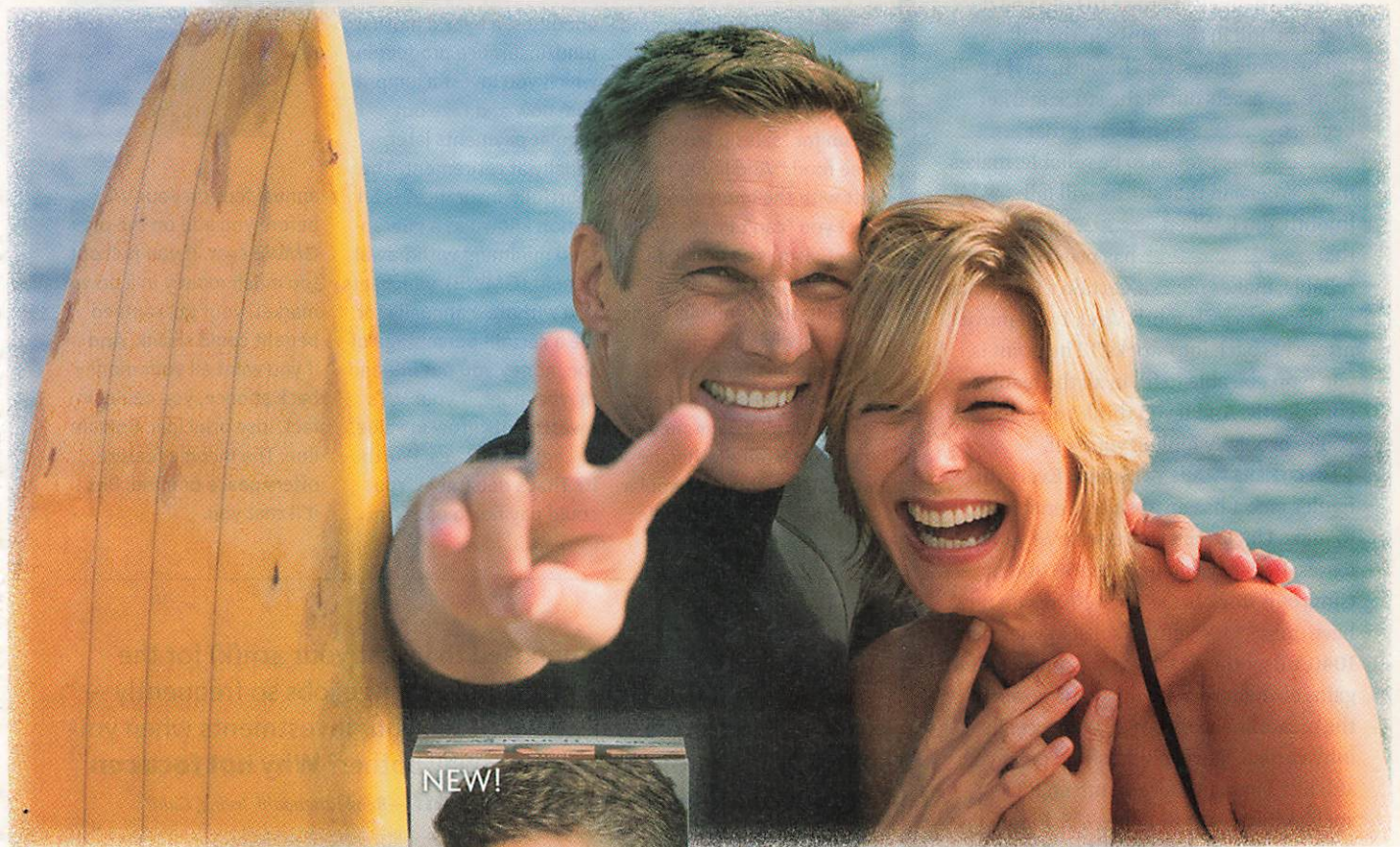
{ **10-YEAR**
ANNUALIZED
RETURNS }

6.1%
DIVERSIFIED PORTFOLIO

NOTES: Figures are through March 31. The diversified portfolio consists of 40% U.S. stocks, 20% foreign stocks, 20% intermediate Treasury bonds, 10% REITs and 10% emerging markets stocks. SOURCE: Morningstar.



The First Hair Treatment That Lets You Keep A Little Gray.



You've got a lot to give. Let it show with New Touch Of Gray™, the only men's hair treatment that lets you



keep a little gray for a great look. Works gradually. Just comb in and rinse.

For The Generation That Refuses To Get Old

feel any more sanguine about being stuck on this desert island of a market. So here are a few other things to think about that might make you feel better while you're waiting for your portfolio to be saved:

> LOOK BEFORE YOU LEAP It's natural to fear that if you do nothing, you will keep losing money. But remember that doing something carries risks of its own. So force yourself to think hard before you act.

Here's a quick exercise to help you do just that. Fill in the blanks in the following two sentences: "On [month, day] I will move my assets out of the stock market because _____, an indicator that _____ has proven to be reliable, makes me _____% certain that stocks will fall _____% by [month, day]. When _____, an indicator that _____ has proven to be reliable, makes me _____% certain that stocks will rise _____% by [month, day], I will move my assets back into stocks." The point is, you won't be able to fill in all the blanks confidently. And if you think you can, you're probably fooling yourself.

> LET OTHERS SHARE YOUR PAIN Every difficult market has an upside: It enables you to make Uncle Sam share some of your losses. Let's say you invested \$5,000 in Citigroup stock in October 2006; you now have only \$2,100 left. So sell. On your next 1040, offset the \$2,900 loss against capital gains elsewhere, reducing your taxes. In the meantime, put the \$2,100 proceeds into a broad-market index fund or (if you still like financial stocks) into an ETF such as iShares Dow Jones U.S. Financial Sector Index (ticker symbol: IYF).

You can do the same with a slumping mutual fund. The net result: You have the same amount invested, and you've taken a big bite out of your current tax bill.

> HAVE COURAGE Finally, look on the bright side—stocks are cheaper now than they've been in years. William Bernstein of Efficient Frontier Advisors puts it this way: "If your friends are running around like recently decapitated poultry, go back in history and look how well stocks did right after things looked the bleakest: 1933, 1974, 1982, 1987"

Those were certainly desolate times. Yet investors who kept putting money to work incrementally in those markets bought their way out. \$

Q Is portfolio insurance legitimate? At a seminar I attended, an adviser said it would cost me 0.5% of what I invest with him. Supposedly it will lock in my gains and I can't lose money no matter what the market does.

—Paula Krensavage, Weirton, W.Va.

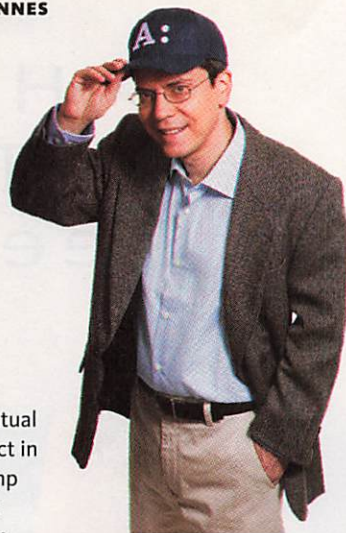
Answer That ringing sound is the alarm bell going off in Answer Guy's brain. "Seminar" is often a euphemism for "sales pitch with free food." And if you're left with the impression that you "can't lose"—well, skepticism is a good idea.

A.G. called the adviser running that seminar. Turns out that what he calls portfolio insurance isn't a way to protect investments so you won't lose money if you cash out. Rather, he was talking about a popular add-on feature of variable

annuities, a hybrid mutual fund/insurance product in which you invest a lump sum now and take out regular payments later, usually at retirement. The "portfolio insurance" is an option known as a guaranteed minimum withdrawal benefit (GMWB), which lets you withdraw annually for life a certain percentage of the money you put in—and maybe more, if your VA's investments grow in value.

Legitimate? Yes. Worth it? That's debatable. You could pay north of 2% in

annual fees on your VA before you add on the 0.5% GMWB cost. If you pull out too much money in a down market, your guaranteed benefit could shrink. And if you want all your money back at once, you could, in fact, lose principal. Bottom line: The income feature offers peace of mind. But it'll cost you.



Q I know you're supposed to invest your 401(k) for the long run. But since people change jobs so frequently—and you usually have to sell your investments when you roll over your 401(k) to an IRA—why bother? **Why not focus on what looks good in the short term?** —René Rosendahl, Irvine, Calif.

Answer Try not to let investment mechanics distract you from investment goals. Remember what the ultimate purpose of the 401(k) is: to provide a tidy sum that will help finance your retirement decades from now. Experience indicates that if you set up a diversified portfolio heavy in stocks, you'll have a good chance of reaching that goal. Success is far less likely if, every time

you switch jobs, you try to guess which market sectors will perform best over the next two or three years. If only it were that easy.

It's true that when you're rolling a 401(k) over into your IRA, you often have to sell investments, take the cash and buy new funds. But that doesn't mean you have to give up on a long-term strategy. All you have to do is find equivalent funds for your

new IRA. For example, if you're selling \$4,000 worth of Brand X large-cap value fund in your old company's 401(k), buy \$4,000 worth of Brand Y large-cap value fund in your rollover IRA. The same thing goes for all the other asset classes in your portfolio. The similarities will likely outweigh the differences between the before and after funds, and you'll be able to stick with the long-term view.



Looking for some answers? Send us your questions about investing. E-mail answer_guy@money.com.

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**JANA PURDY
and TIM KRAMER**

LAKEWOOD, COLO.
JANA, 61, TIM, 48

GOALS

- ☐ RETIRE TOGETHER IN LESS THAN FIVE YEARS
- ☐ SIMPLIFY THEIR FINANCES
- ☐ BE ABLE TO WINTER IN FLORIDA OR CALIFORNIA

ASSETS

- ☐ \$630,000 IN RETIREMENT ACCOUNTS
- ☐ \$595,000 IN TAXABLE INVESTMENTS
- ☐ \$550,000 IN HOME EQUITY
- ☐ \$50,000 IN EMERGENCY SAVINGS



A May-December Retirement Plan

Separated by 13 years, these big savers want to know whether they can afford to retire together **BY JOE LIGHT**

JANA PURDY, 61, JOKES THAT SHE ROBBED THE CRADLE WHEN SHE nabbed her husband Tim Kramer, 48. The pair met in a volleyball league, and they got married just before a tournament in 1988. For the past 20 years, their age difference was more of an amusement than a challenge. But with Jana hoping to retire soon—in less than five years—the couple are starting to worry if it might complicate their plans. After all, when she turns 66, Tim will be only 53. Yet Tim still

hopes to quit at the same time as Jana. “We’ve tried to look at retirement calculators and programs that would let us know what we can do, but they try to squeeze every kind of couple into a shoebox,” he says. “We don’t fit into that shoebox.”

WHERE THEY ARE NOW

Fortunately, this couple took retirement savings seriously and started socking away money decades ago. On their combined annual income of around \$120,000, Tim, an engineer for a safety-equipment

company, and Jana, who runs her own small law practice, have accumulated \$1.2 million. With no kids, these world-class savers are socking away some \$45,000 a year—more than a third of their income—by maxing out their 401(k)s and IRAs and saving additionally in a sprawling collection of taxable investments and variable annuities. Tim is also vested in pensions through his current and a former employer. What's more, they have around \$550,000 in equity in their Lakewood, Colo. home and a nearby condo they own and rent out to Jana's sister Pam.

Still, it's a challenge to keep up this savings pace. In 2006, Jana was diagnosed with chronic fatigue syndrome. The illness forced her to scale back her work and added \$16,000 in annual unreimbursed medical expenses.

WHAT THEY SHOULD DO

> Time their withdrawals properly. Once they pay off their modest mortgage in three years, Tim estimates that he and his wife can get by on about \$43,000 a year. But they want to live a little larger once they ditch their jobs. At the very least, they hope to spend winters near family in Florida or California. "My illness has made me really cold-sensitive, and Colorado winters are tough," Jana says.

Doing so will probably push their annual income requirement up to \$80,000, says Karlton Childress, a Denver-based financial planner. But that's still a realistic target—even if Tim retires early, Childress says. Assuming Jana and Tim retire in five years, market appreciation and their ongoing savings should push their nest egg to nearly \$2.1 million, Childress says. That, plus Jana's Social Security benefits—which she'll start tapping at 66—should be more than enough to generate \$80,000 a year safely. It should also allow Tim to wait until his mid-sixties to draw on his pensions and avoid having to settle for a permanent early-retirement reduction in his monthly benefits.

> Unravel their variable annuities. Lured by the promise of "guaranteed returns," Tim and Jana are investing in two variable annuities. But Childress thinks their accounts' high fees make them bad long-term investments. The first annuity, which

they purchased six years ago, has a value of \$115,000. Its surrender charge has steadily dropped from 8% to 5% over the past few years. Once it hits zero, Childress recommends they get out of it.

> Streamline their investments. Childress says the couple are on target with their investment mix, with roughly 70% of their portfolio in stocks and 30% in bonds. Their real problem is how chaotic their portfolio is. Between them, Tim and Jana own about 90 funds and stocks spread among three brokerage accounts, three IRAs, two 401(k)s, two variable annuities and an old-fashioned Keogh account.

Most troubling is the fact that Tim and Jana keep almost \$215,000 in brokerage accounts they use to trade stocks.

Childress suggests they trim that down to \$50,000 of "play money." The rest would be better off in diversified funds, like **Vanguard Total Stock Market** (ticker symbol: VTSMX) or **Vanguard Total International Stock** (VGTIX), which they can buy and hold.

Tim, the stock picker of the two, thinks he's doing just fine trading securities in those accounts. But Jana is in favor of liquidating at least her share. "If we're looking to retirement, let's 'play' with less money," she says, "and invest in things that we don't have to spend as much time watching." \$

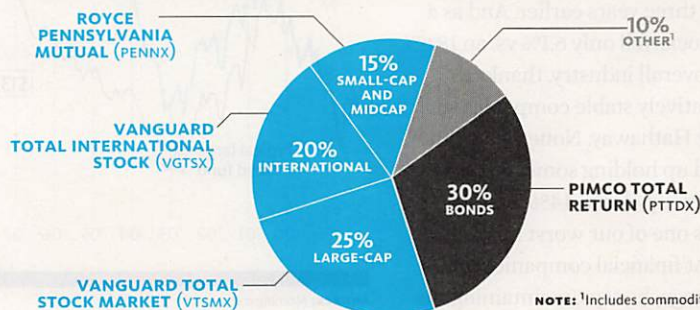
 Want a MONEY Makeover? E-mail us at makeover@money.com.

THE MAKEOVER

	THE PROBLEM	THE PLAN	THE PAYOFF
1	Tim, who's 13 years younger than Jana, will need to support himself for many more years if they retire together.	Retire together but use only their retirement savings and Jana's Social Security benefits to generate income early on.	By relying on these sources first, Tim can delay tapping his pensions, maximizing the benefits to cover his long life expectancy.
2	The couple set aside nearly a fifth of their \$1.2 million nest egg to trade, a risky strategy.	Liquidate most of those accounts and reinvest the money instead in low-cost mutual funds they can buy and hold.	Not only will this keep their trading to a minimum, it will simplify their portfolio of stocks and funds.
3	Lured by "guaranteed returns," they're invested in two high-fee variable annuities.	Pull the money out once the surrender charges disappear, and invest in low-cost mutual funds.	They'll free themselves of the high fees that are cutting into their returns.

THE PORTFOLIO

This mix will keep the couple's money growing to cover Tim's life expectancy.



NOTE: ¹Includes commodities and real estate.

Sound Thinking for a Shaky Market

Veteran fund manager Chris Davis isn't one to panic. Here he explains why you shouldn't either.

▶ **During times of market turmoil,** it helps to get perspective from a truly savvy Wall Street veteran—someone like Chris Davis, lead manager of \$11.3 billion Selected American Shares, a MONEY 70 fund. Davis follows a long tradition of investing success. His grandfather, Shelby Cullom Davis, built a fortune in insurance stocks, and his dad, Shelby Davis, who founded the Davis Selected fund group, had one of the best fund track records in the business. Chris Davis himself is no slouch—Selected American, which he co-manages with Ken Feinberg, has outpaced nearly 90% of large-cap stock funds over 10 years, employing a buy-and-hold strategy that many competitors can't muster the conviction to follow. Davis doesn't speak to the press much, but when I sat down with him recently to talk about navigating today's uncertain markets, he had plenty of smart things to say that apply whether you're managing billions or thousands. His key points:

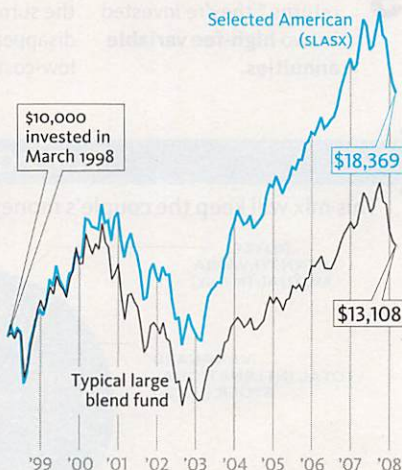
▶ **Realize that you can't know everything.** No matter how much expertise you have, you will be caught by surprise. Take financial stocks. Despite his long history with them, Davis did not fully anticipate the widespread losses by financials as a result of the subprime mess. True, the fund had trimmed back its financial stake to about 30% of assets last year from a high of 50% three years earlier. And as a group, his stocks fell only 6.1% vs. an 18.6% loss for the overall industry, thanks to stakes in relatively stable companies such as Berkshire Hathaway. Nonetheless, the fund did end up holding some disasters—notably Citigroup, down 44% in 2007. "Citigroup is one of our worst mistakes," Davis says. At financial companies that take on leverage, he says, maintaining the

right corporate culture is essential to controlling risk. But, Davis says, he and Feinberg overlooked signs of trouble at Citi, including the exit of top executives and a change in the chief financial officer position. To be fair, Davis and Feinberg had started reducing their stake in Citi in 2006—recently the stock accounted for just 1% of the portfolio.

▶ **Bear markets offer some terrific bargains—but be careful.** "My grandfather always said, 'You make most of your money during a bear market; you just don't realize it at the time,'" Davis recalls. After all, it's when times are bad that you can scoop up quality stocks at discount prices. But buying into a falling market

PATIENCE IS MORE THAN ITS OWN REWARD

Selected American's buy-and-hold managers separated from the pack when stocks started falling, and they've since increased their lead.



SOURCE: Morningstar.



requires steely nerves—and plenty of patience. In December, Davis paid \$48 a share for a 4% stake in Merrill Lynch, which has suffered steep subprime losses. "I'm always looking for a trifecta—the right business with the right management at the right price," says Davis. "I've been studying Merrill Lynch for 15 years, and it never fit all three criteria till now." Davis believes that the value of Merrill's wealth-management business, including its vast network of advisers, outweighs its current problems. He is a big fan of new CEO John Thain, who turned around the New York Stock Exchange. And the stock trades for half what it did a year ago. Still, Davis is not counting on a quick rebound in either Merrill or other financial stocks. "This is not the time to back up the truck in financials," he says. "It's important to be careful about what you buy, since it's a dangerous time. Things may go lower from here." Recently, in fact, Merrill shares were trading at just \$44 a share. But Davis maintains that price declines in the stock will only create an opportunity to buy more.

▶ **Sometimes it's better to just sit on your hands.** Although Davis and Feinberg are constantly on the hunt for new opportunities, they rarely pull the trigger, either to buy or sell. Stocks typically remain in the



NOTES FROM YOUR FUTURESELFTM



IF YOUR FUTURESELF COULD TALK TO YOU, WHAT WOULD IT SAY?

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Fund Watch

fund's portfolio for eight years or more, even during times when returns lag, as long as the managers continue to have faith in the company's strategy. "You have to give your investments time to work, and you have to expect years of underperformance," says Davis. "For the average investor, the keys to wealth are stay disciplined, keep averaging in and not try to time the market." That's exactly what Davis is doing with the bulk of the fund's

longtime holdings—blue-chip stocks that offer steady growth. Many of those companies, such as Procter & Gamble and General Electric, earn 45% or more of their earnings abroad, which provides overseas exposure as well. These stocks have been largely overlooked in recent years, Davis notes, as investors have chased higher returns from other asset classes, such as hedge funds and emerging markets. But those investments often

carry high costs and high risk—and lately their returns have slumped. As a result, investors may finally start paying attention to the steady returns of blue chips. Says Davis: "I think the story of the next five years will be the comeback of U.S. multinational stocks." Given the investing time horizon of the Davis funds, that wouldn't be a long wait. **\$**

FEEDBACK: pwang@money.com

Money70

OUR LIST OF RECOMMENDED MUTUAL FUNDS AND ETFs

MONEY 70 stock funds rebounded in the month ended April 17, following a down performance in March. Rising oil prices made commodity funds the big winners, with **T. Rowe Price New Era** up 17.8%. Emerging market funds also did well. Bond funds' performance sagged, however, on worries about rising inflation and the continuing credit crunch. The biggest loser was the **iShares Lehman TIPS Bond** fund, down 2.1%.

FUND (TICKER)	TOTAL RETURN			EXPENSES (AS % OF ASSETS) ¹	PHONE NUMBER (800)
	1MO.	1YR.	3YRS. ¹		
Large-Cap					
American Funds Amcap (AMCPX) ³	1.0%	-6.1%	6.3%	0.64	421-0180
American Funds Am. Mutual (AMRMX) ³	2.0	-6.3	7.4	0.56	421-0180
Fairholme (FAIRX)	5.1	7.3	13.9	1.00	202-2263
Fidelity Spartan 500 Index (FSMIX)	2.9	-5.4	7.6	0.10	343-3548
Fidelity Spartan Total Market (FSTMX)	3.4	-5.7	8.2	0.10	343-3548
FMI Large Cap (FMIHX)	2.2	-3.9	8.8	1.00	811-5311
iShares S&P 500 Index (IVV)	2.8	-5.3	7.6	0.09	474-2737
Jensen (JENSX)	-0.2	-2.1	4.5	0.85	992-4144
Matrix Advisors Value (MAVFX)	1.8	-9.1	6.0	0.99	366-6223
Selected American (SLASX)	4.8	-3.9	8.7	0.88	243-1575
Sound Shore (SSHFX)	3.1	-6.3	8.2	0.92	551-1980
T. Rowe Price B/C Growth (TRBCX)	3.2	-2.7	8.2	0.77	638-5660
T. Rowe Price Equity Income (PRFDX)	1.8	-7.0	7.5	0.69	638-5660
Vanguard 500 Index (VFINX)	2.8	-5.4	7.5	0.18	851-4999
Vanguard Total Stock Market (VTSMX)	3.4	-5.7	8.1	0.18	851-4999
Vanguard Total Stock Market ETF (VTI)	3.4	-5.6	8.2	0.07	851-4999
Vanguard Windsor II (VWNFX)	3.1	-10.7	6.6	0.32	851-4999
Midcap					
FAM Value (FAMVX)	-0.4	-11.4	3.2	1.18	932-3271
Fidelity Value (FDVLX)	4.7	-10.3	9.1	0.69	343-3548
FPA Perennial (FPPFX) ⁴	0.6	-6.7	4.7	0.92	982-4372
Janus Mid Cap Value (JMCVX)	3.5	-1.3	11.4	0.85	525-3713
Meridian Growth (MERDX)	1.4	-11.4	6.5	0.84	446-6662
Primecap Odyssey Agg. Gro. (POAGX)	3.8	-16.3	7.7	0.78	729-2307
Vanguard Mid-Cap ETF (VO)	6.5	-7.0	10.3	0.12	851-4999
Vanguard Mid-Cap Index (VIMSX)	6.5	-7.1	10.2	0.22	851-4999
Multicap					
Bridgeway Agg. Inv. 2 (BRAIX)	12.8	11.1	16.6	1.21	661-3550
Muhlenkamp (MUHLX)	4.0	-16.9	-0.4	1.04	860-3863
Weitz Hickory (WEHIX)	1.5	-23.1	0.6	1.20	304-9745
Small-Cap					
Bridgeway Small Cap Value (BRSVX)	5.4	-6.9	11.1	0.83	661-3550
Royce Pennsylvania Mutual (PENNIX)	4.5	-7.0	10.0	0.87	221-4268
Royce Value Plus (RYVPX)	5.7	-11.5	12.6	1.33	221-4268
T. Rowe Price New Horizons (PRNHX)	4.5	-10.3	6.4	0.80	638-5660
Vanguard Small-Cap ETF (VB)	4.8	-10.4	8.0	0.09	851-4999
Vanguard Small-Cap Index (NAESX)	4.8	-10.5	7.9	0.23	851-4999
Specialty					
Cohen & Steers Realty (CSRSX)	4.3	-14.1	13.6	0.96	330-7348
iShares Dow Jones Select Div. (DVI)	-0.3	-15.6	3.8	0.40	474-2737

FUND (TICKER)	TOTAL RETURN			EXPENSES (AS % OF ASSETS) ¹	PHONE NUMBER (800)
	1MO.	1YR.	3YRS. ¹		
Specialty continued					
iShares S&P GSSI Nat. Res. Index (IGE)	16.1%	31.2%	27.2%	0.48	474-2737
Third Ave. Real Estate Value (TAREX)	2.4	-17.3	8.6	1.11	443-1021
T. Rowe Price New Era (PRNEX)	17.8	36.4	29.9	0.64	638-5660
Vanguard REIT ETF (VNQ)	4.9	-12.5	13.5	0.11	851-4999
Vanguard REIT Index (VGSIX)	4.9	-12.5	13.4	0.21	851-4999
Foreign					
Am. Funds Euro Pacific Gro. (AEPGX) ³	7.1	6.2	19.0	0.75	421-0180
American Funds New World (NEWFX)	7.5	18.1	27.7	0.96	421-0180
Artisan International (ARTIX)	7.8	1.9	17.6	1.20	344-1770
Dodge & Cox Intl. Stock (DODFX)	6.4	-4.9	15.6	0.65	621-3979
Fidelity Spartan International (FSIIX)	7.8	-2.8	15.1	0.09	343-3548
Oakmark International (OAKIX)	4.7	-16.1	9.9	1.05	625-6275
Third Avenue International Value (TAVIX)	5.6	1.9	12.0	1.45	443-1021
T. Rowe Price Emerging Markets (PRMSX)	10.9	27.1	34.7	1.20	638-5660
T. Rowe Price Intl. Discovery (PRIDX)	5.8	-2.3	19.8	1.21	638-5660
Vanguard Emerging Mkts. ETF (VWO)	11.2	23.9	31.6	0.24	851-4999
Vanguard Emerging Mkts. Stock (VEIEX)	11.2	23.7	31.4	0.37	851-4999
Vanguard Europe Pacific ETF (VEA)	8.8	N.A.	N.A.	0.12	851-4999
Vanguard FTSE All-World ex-U.S. (VEU)	8.8	3.1	N.A.	0.24	851-4999
Vanguard International Growth (VWIGX)	9.5	2.6	17.5	0.51	851-4999
Vanguard Total Intl. Stock (VGTSX)	8.6	1.5	17.6	0.32	851-4999
Bond					
American Funds Amer. H/I (AHITX) ⁵	3.2	-3.5	5.7	0.66	421-0180
Dodge & Cox Income (DODIX)	-0.1	3.5	4.2	0.44	621-3979
FPA New Income (FPNIX) ⁶	-0.4	5.8	4.6	0.62	982-4372
Harbor Bond (HABDX)	-0.5	9.7	5.7	0.56	422-1050
iShares Lehman TIPS Bond (TIP)	-2.1	12.8	5.6	0.20	474-2737
T. Rowe Price Intl. Bond (RPIBX)	-0.2	15.9	6.2	0.82	638-5660
Vanguard Infl.-Pro. Securities (VIPSX)	-1.8	13.0	5.7	0.20	851-4999
Vanguard Intm.-Term T/E (VWITX)	1.1	3.9	3.7	0.15	851-4999
Vanguard Short-Term Bond (VBISX)	-0.9	7.7	5.0	0.18	851-4999
Vanguard Short-Term Bond ETF (BSV)	-1.1	7.9	N.A.	0.09	851-4999
Vanguard Total Bond Market (VBMFX)	-1.2	6.3	4.8	0.20	851-4999
Vanguard Total Bond Market ETF (BND)	-1.0	6.6	N.A.	0.09	851-4999
Target-Retirement					
T. Rowe Price Retirement (STOCK/BOND ALLOCATION)					638-5660
2005 Fund (55%/45%) (TRRFV)	2.0	-0.1	7.7	0.60	
2020 Fund (80%/20%) (TRRBX)	3.4	-3.4	8.7	0.69	
Vanguard Target Retirement					851-4999
2025 Fund (79%/21%) (VTTVX)	3.2	-1.9	7.8	0.19	
2035 Fund (90%/10%) (VTTHX)	3.8	-3.1	8.6	0.19	

NOTES: As of April 17. N.A.: Not available. Load funds are included for those who prefer to use a broker. ¹Annualized. ²Audited and annualized figures except on Fidelity. ³5.75% sales load. ⁴Area code is 866. ⁵5.25% sales load. ⁶Area code is 877. SOURCES: Lipper, New York, 877-955-4773; the fund companies.



IT'S SMART, BEAUTIFUL AND CAN TELL YOU EXACTLY WHAT TO DO.

THE ALL NEW CHEVY MALIBU



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Stock Buyers Breathe a Sigh of Relief

Blue chips post modest gains on hopes that the worst is nearly over

▶ **The economy remains weak**, but investors are starting to think that the financial system has already suffered the worst of the fallout from the subprime mortgage fiasco. As a result, battered blue chips have come back a bit.

For the month ended April 18, Sivy 70

gainers led losers by 2 to 1. Winners included Schlumberger on higher oil prices; Lowe's and Wal-Mart on hopes of improving sales; and Citigroup after an earnings report that wasn't as awful as it might have been. Big decliners included Applied Materials on projections that semiconductor

sales would deteriorate; General Electric after a lousy earnings report; and Northrop Grumman, which has problems in its shipbuilding division. **\$**

At cnmoney.com/sivy you can see the latest Sivy 70 data. E-mail editor-at-large Michael Sivy at msivy@money.com.

Sivy 70

BLUE-CHIP GROWTH STOCKS FOR THE LONG RUN

STOCK (TICKER)	PRICE	1-MONTH RETURN	12-MONTH RETURN	P/E RATIO	EARNINGS GROWTH	YIELD	STOCK (TICKER)	PRICE	1-MONTH RETURN	12-MONTH RETURN	P/E RATIO	EARNINGS GROWTH	YIELD
Abbott Laboratories (ABT)	\$50.93	-4.7%	-9.9%	15.8	12%	2.8%	Home Depot (HD)	\$28.12	3.4%	-25.7%	15.8	12%	3.2%
Aetna (AET)	41.36	-2.0	-9.7	10.3	15	0.1	IBM (IBM)	123.08	3.9	31.5	14.4	10	1.3
AFLAC (AFL)	67.40	5.4	39.6	17.0	15	1.4	Illinois Tool Works (ITW)	51.04	4.6	0.6	14.3	12	2.2
Alcoa (AA)	35.57	-7.8	5.2	12.3	15	1.9	Intel (INTC)	22.11	1.7	5.7	17.6	15	2.5
American Express (AXP)	44.70	2.7	-22.4	13.4	12	1.6	InterActiveCorp (IAC)	20.65	-0.2	-46.4	12.8	14	0.0
Amgen (AMGN)	42.63	3.4	-29.0	10.2	10	0.0	Johnson & Johnson (JNJ)	65.76	0.7	4.6	14.8	7	2.5
Anadarko Petroleum (APC)	67.34	4.0	46.4	14.8	7	0.5	Johnson Controls (JCI)	33.90	1.4	6.4	13.8	14	1.5
Anheuser-Busch (BUD)	48.31	4.5	-4.9	16.0	8	2.7	J.P. Morgan Chase (JPM)	45.12	6.5	-10.4	13.8	9	3.4
Applied Materials (AMAT)	19.17	-11.0	-1.4	18.9	15	1.3	Lilly (LLY)	51.39	2.9	-10.2	13.0	7	3.7
Automatic Data Proc. (ADP)	43.43	7.7	-1.1	20.0	15	2.7	Limited Brands (LTD)	17.84	7.5	-30.3	12.7	13	3.4
Bank of America (BAC)	37.47	-3.8	-22.9	11.4	7	6.8	Lowe's (LOW)	24.53	10.0	-21.0	15.9	15	1.3
Best Buy (BBY)	42.49	3.4	-12.1	13.4	15	1.2	Merrill Lynch (MER)	46.71	0.2	-46.9	24.2	12	3.0
Boeing (BA)	76.91	0.5	-16.5	13.0	13	2.1	Microsoft (MSFT)	29.22	-0.7	3.6	15.6	12	1.5
Burlington Northern (BNI)	97.89	3.1	8.0	16.6	14	1.3	Nike (NKE)	67.55	9.5	26.9	18.6	13	1.4
Caterpillar (CAT)	78.59	2.7	15.8	13.3	12	1.8	Northrop Grumman (NOC)	71.07	-10.9	-4.3	13.5	14	2.1
Cisco Systems (CSCO)	23.89	-6.6	-11.1	15.5	14	0.0	Omnicom Group (OMC)	45.30	4.4	-12.3	13.7	12	1.3
Citigroup (C)	24.03	16.0	-51.0	20.2	9	5.3	PepsiCo (PEP)	70.77	1.1	9.6	19.0	11	2.1
Coca-Cola (KO)	60.68	2.1	20.2	19.8	9	2.5	Pfizer (PFE)	20.40	-2.9	-19.4	8.5	4	6.3
Colgate-Palmolive (CL)	77.70	0.1	18.6	20.3	11	2.1	Procter & Gamble (PG)	67.56	-0.8	8.8	19.3	12	2.4
Comcast (CMCSA)	20.16	4.3	-27.3	22.7	13	1.2	Schlumberger (SLB)	95.30	13.0	28.2	19.8	20	0.9
ConocoPhillips (COP)	82.81	5.8	21.0	7.8	10	2.3	Staples (SPLS)	22.34	1.2	-14.5	14.8	14	1.5
Corning (GLW)	25.40	4.1	8.1	14.5	16	0.8	Sysco (SYS)	28.02	-2.7	-13.8	15.8	13	3.1
CVS (CVS)	40.42	3.1	17.8	16.3	17	0.6	Target (TGT)	53.41	4.7	-11.3	15.2	15	1.0
Danaher (DHR)	74.16	-2.4	3.2	17.0	13	0.2	Texas Instruments (TXN)	28.79	-2.3	-8.8	14.6	15	1.4
Disney (DIS)	30.78	-3.0	-9.1	13.7	13	1.1	3M (MMM)	80.65	-0.4	7.1	14.8	11	2.5
DuPont (DD)	51.21	7.9	7.1	14.7	9	3.2	Time Warner (TWX)	14.61	1.9	-28.7	13.4	13	1.7
ExxonMobil (XOM)	93.38	5.5	21.2	11.1	6	1.5	T. Rowe Price (TROW)	53.75	9.4	7.1	22.0	14	1.8
FedEx (FDX)	94.96	9.2	-11.6	15.6	14	0.4	Union Pacific (UNP)	135.55	4.8	20.5	16.6	14	1.3
Fortune Brands (FO)	70.85	8.9	-8.7	14.4	10	2.4	UnitedHealth Group (UNH)	36.70	4.8	-32.2	9.5	15	0.1
Genentech (DNA)	73.31	-6.5	-10.7	21.4	22	0.0	United Technologies (UTX)	70.79	1.4	7.6	14.6	12	1.8
General Dynamics (GD)	86.21	1.4	13.5	15.0	10	1.6	Viacom (VIAB)	40.02	1.5	-3.7	15.0	13	0.0
General Electric (GE)	32.02	-11.4	-5.5	14.4	11	3.9	Walgreen (WAG)	35.73	-3.0	-21.5	16.1	15	1.1
Harley-Davidson (HOG)	36.09	-2.0	-39.2	10.1	11	3.3	Wal-Mart (WMT)	56.67	11.2	20.0	16.5	12	1.7
Hershey (HSY)	35.69	-2.0	-32.4	19.4	7	3.3	Wells Fargo (WFC)	29.71	-5.8	-14.0	12.6	10	4.2
Hewlett-Packard (HPQ)	47.31	-1.3	16.2	13.4	14	0.7	Wyeth (WYE)	43.81	7.4	-20.3	12.8	3	2.6

NOTES: As of April 18. P/E ratios are based on projected earnings for 2008. Earnings growth is the compound annual rate projected for five years by analysts covering the stock.

↑ Up 10% or more for the month. ↓ Down 10% or more for the month. SOURCE: Thomson/Baseline.

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Mailbox Size	2000 MB	500 MB	75 MB
Website Builder	12 Pages	Additional \$8.09/month	✓
Access to Open Source Application Library	✓	✓	—
Starter Software Suite	✓	—	—
Search Engine Submission	✓	—	—
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Yes, it's a tough market, but don't assume you need more "weapons" in your portfolio. Now more than ever, don't complicate your strategy. Simplify it.

BY MICHAEL SIVY, CARLA FRIED, CAROLYN BIGDA AND
GEORGE MANNES PHOTOGRAPHS BY CRAIG CUTLER

Investments

YOU NEED

THE BIG MYTH IN INVESTING is this: Managing your portfolio in this market is some kind of complicated, arcane science. It isn't, but it's easy to see why many people believe it is. For one thing, the misconception is repeated daily by TV stock touts, talk-radio hosts and the armies of financial salesfolk whose jobs depend on overstating the value they add. Also, basic stocks and bonds—the elements of a simple portfolio—have not performed as well lately as abstruse assets like hedge funds or commodities, a point relentlessly raised by the people selling these items.

Best advice: Turn off the noise and focus on your true goals. You are not a Wall Street pro whose bonus depends on beating the market every quarter. All you need to do is make sure your portfolio stays on target to meet future needs, like your kids' education or your own retirement. You don't have unlimited time to research stocks and review relative valuation models for odd asset classes. You'll make much better decisions if you hold your investments to a number small enough to track and under-

stand easily, but large enough that you're not putting all your eggs in one economic basket. The precise number is debatable, but there is plenty of research to suggest that your portfolio need not hold any more than seven basic asset classes—each of which can be covered by a single mutual fund. That's right, seven investments is all it takes.

How can a simple mix like that compete in a tough market when it leaves out the hot assets of the day? "This question always comes up when there's turmoil," says John Markese, president of the American Association of Individual Investors. "But unless you can perfectly time the market in gold or oil—and nobody can—complicating your portfolio won't improve your returns." Research by Ibbotson Associates confirms as much. Between 1972 and 2007, a portfolio of 60% stocks, 30% bonds and 10% cash returned 10.7% a year. That same general mix, with small amounts taken from stocks and added to commodities, gold and real estate, gained exactly the same.

But does a mix of just seven offer sufficient diversification? It does if it's the right seven. When you invest in funds like the seven recommended in the next few pages, you own pieces of hundreds of companies all over the world. As a result, you don't need a separate sum in, say, commodities: The natural-resources and energy stocks in broadly diversified equity funds give you indirect exposure to those assets. And as long as you adjust the share of your portfolio devoted to each category—shifting more to bonds and cash as you age, for example—these seven can serve you for a long, long time.

Remember: The research on diversification suggests that your portfolio needs no more than seven asset classes. Other research is clear on what kind of individual investments should fill each category. As Harvard economist Gregory Mankiw puts it, "Put your faith in tax-efficient index funds." Accordingly, our top choices (with one key exception) are index funds, designed to match broad market benchmarks.

Will they make you the toast of your next cocktail party? Probably not. But they represent a strategy confirmed and reconfirmed as the one that really works in investing—and one you don't have to be a Wall Street genius to follow. In a market like today's, practical beats sexy. It's that simple.

1 A BLUE-CHIP U.S. STOCK FUND

FIRST CHOICE FIDELITY SPARTAN 500 INDEX (FSMKX)

➤ NOT SO LONG AGO, the idea that U.S. stocks should be at the core of any investment strategy would have been deemed too obvious to discuss. This decade, in which the brutal 2000-02 bear market and the current downturn

have left the S&P 500 stuck where it started, may have changed that. Let's review: Since 1967 there have been seven bear markets, with losses ranging from 19% to 49%. Even so, the annual gain for blue-chip U.S. stocks is 10.8%—far outpacing bonds. Those painful but temporary losses are the price you pay for higher potential returns. And those gains are the best defense against the corrosive effects of inflation. Are stocks better than gold at whipping inflation? Way better: Since 1908, stocks have grown more than eightfold after inflation; gold has little more than doubled in today's dollars. Although U.S. firms no longer dominate the world, their stocks still account for more than 40% of the world's equity value. So U.S. blue chips need to be at the heart of a diversified strategy. The best way to own them is through the Fidelity Spartan 500 Index fund. It replicates the performance of the S&P 500 and takes only a sliver of a fee for doing so: 0.10% a year.

FIDELITY SPARTAN 500 INDEX

	FUND	CATEGORY
5 YEAR RETURN	11.2%	11.2%
10 YEAR RETURN	3.7%	3.9%
ANNUAL EXPENSES	0.1%	1.3%

NOTE: Returns are annualized.
SOURCE: Morningstar.

ALTERNATIVES iShares S&P 500 Index (IVV) and Selected American Shares (SLASK)

2 A BLUE-CHIP FOREIGN-STOCK FUND

FIRST CHOICE VANGUARD TOTAL INTERNATIONAL STOCK INDEX (VTGSX)

➤ THE MOST IMPORTANT REASON you need to own foreign stocks has nothing to do with the fact that they've trounced U.S. equities for the past five years. Sticking only with domestic stocks is akin to shopping in a store that's missing most of its inventory: Nearly 60% of the world's stock market value resides

in companies outside our borders. Besides, since investing in stocks is all about owning a piece of a growing economic pie, you have to go to where the growth is—and 76% of the world's economic activity takes place outside the U.S. Then there's the diversification argument. Even though foreign markets held up no better than U.S. ones in the current downturn, overseas diversification still works. Researchers at T. Rowe Price found that since 1970, a 20% weighting in foreign equities both raised a U.S. fund

VANGUARD TOTAL INTERNATIONAL STOCK INDEX

	FUND	CATEGORY
5 YEAR RETURN	23.0%	20.0%
10 YEAR RETURN	7.4%	5.7%
ANNUAL EXPENSES	0.3%	1.5%

NOTE: Returns are annualized.
SOURCE: Morningstar.

portfolio's return and cut its risk. The simplest way to add stocks from both developed and emerging economies to your portfolio is to own Vanguard Total International Stock Index. As an index fund, it merely aims to match the return of the world's stock markets. Thanks to the inherent wisdom and efficiency of this approach—the fund charges a tiny 0.27% a year in expenses—it has outperformed more than 90% of its peers over the past five years.

ALTERNATIVES Vanguard FTSE All World Ex-U.S. ETF (VEU) and Dodge & Cox Intl. Stock (DODFX)



3 A SMALL-COMPANY FUND

FIRST CHOICE **T. ROWE PRICE NEW HORIZONS** (PRNHX)

> **THE GREATEST RETURNS** in the stock market come from taking above-average risks. That's why over periods of a decade or longer, small-company funds—which own shares of small, dynamic companies—can outpace the rest of the market by an average of one to three percentage points a year. This isn't the only

T. ROWE PRICE NEW HORIZONS

	FUND	CATEGORY
5 YEAR RETURN	14.8%	13.1%
10 YEAR RETURN	6.0%	4.6%
ANNUAL EXPENSES	0.8%	1.6%

NOTE: Returns are annualized.
SOURCE: Morningstar.

reason to carve out a permanent niche in your portfolio for such funds. They sometimes pick up steam just when blue chips stagnate, making them a great diversifier. In the 1970s, for instance, small stocks delivered nearly twice the gains of blue chips. "Adding that small-cap performance gives you a nice extra bit of diversification," says Frank Armstrong, founder of the advisory firm Investor Solutions.

This category makes particular sense when you're decades from needing to tap your

portfolio. The farther off that goal, the more time you have to benefit from small-stock funds' long-term growth, and the less you need to worry about their periodic nosedives. Most of our first-choice picks are index funds, but this one is an exception: T. Rowe Price New Horizons. In this category, it may be worth paying slightly more—just slightly—for active management, and New Horizons is one of the most efficient of the actively managed crowd.

ALTERNATIVES **Vanguard Small-Cap Index** (NAESX) and **Vanguard Small-Cap ETF** (VB)

4 A VALUE FUND

FIRST CHOICE **VANGUARD VALUE INDEX** (VIVAX)

> **THE UNIVERSE OF EQUITIES** is divided into two groups: growth stocks, which are shares of high-performing companies that often trade at steep prices (relative

VANGUARD VALUE INDEX

	FUND	CATEGORY
5 YEAR RETURN	13.4%	12.0%
10 YEAR RETURN	4.6%	4.8%
ANNUAL EXPENSES	0.2%	1.3%

NOTE: Returns are annualized.
SOURCE: Morningstar.

to their earnings growth or assets); and value investments, overlooked or beaten-down shares selling at discount prices. Why do you need to bother with the bargain-basement bin? For starters, value stocks typically pay out significantly higher dividends than growth companies. Today, in fact, the average value stock in the S&P 500 yields 3.5%—nearly twice what growth stocks pay out. Dividends give value stocks a steadier source of return than growth funds, which rely almost entirely on the market's opinion. That's one

reason that over long stretches, value trumps growth more often than not. In the equity investors' bible, *Stocks for the Long Run*, University of Pennsylvania professor Jeremy Siegel points out that value returned an average of 15.7% a year between 1975 and 2001, nearly two points a year more than growth stocks.

When choosing a value fund, the last thing you want to do is overpay. Vanguard Value Index is a cost-effective way to buy the universe of blue-chip value stocks for just 0.20% in annual fees. The low costs explain how this plain-vanilla fund has returned about 13% a year since 2003, beating 78% of its peers.

ALTERNATIVES **iShares S&P 500 Value Index** (IVE) and **T. Rowe Price Equity Income** (PRFDX)

HOW TO UNCOMPLICATE YOUR INVESTMENTS

If you're just starting out as an investor, keeping it simple is, well, pretty simple. Just assemble a portfolio from the seven funds on our list (or similar ones if your 401(k) doesn't offer our picks). But odds are you've already been saving and investing for years, and you may well own a collection of funds and ETFs—and perhaps a few individual stocks to boot—that seem more like a messy attic than an elegant portfolio. Especially if you can't quite remember why you own particular stocks or funds, you'll want to prune them back to the seven categories described in this story. But do so cautiously and systematically, since you could trigger capital-gains taxes if you rush into things.

STEP 1 > Start the process within your 401(k)s and IRAs. Since trades within these accounts don't trigger capital-gains taxes, you can consolidate your portfolio relatively painlessly. You may have to pay a commission on some trades, but the simplification should be worth it. "You could find your portfolio is both easier to track and less costly to boot," says Rande Spiegelman, vice president of financial planning at Schwab. Also, if you have 401(k)s from prior jobs, roll those over into your IRA. It's that many fewer accounts to keep track of.

STEP 2 > Use today's turbulent market to edit your holdings. Take a look within your taxable accounts for investments that are now worth less than you paid for them, thanks to the recent sell-off. If you get rid of those now, you get two benefits: You can take the proceeds of the sale and roll them into your simplified portfolio without incurring taxes. Plus, your capital losses will offset gains you'll incur when you sell other funds—or reduce your income taxes next April.

STEP 3 > Stop further complicating matters. If you have random mutual funds you aren't ready to sell because you don't want to face the taxes, at least stop reinvesting distributions back into them. Direct the money instead into the simple portfolio. That way, when you are ready to sell, there will be less to unload.

5 A HIGH-QUALITY BOND FUND

FIRST CHOICE **VANGUARD TOTAL BOND MARKET INDEX (VBMFX)**

AS MUCH AS YOU NEED STOCKS, “precious few people can really stomach an all-stock portfolio,” says William Bernstein, author of *The Four Pillars of Investing*. Equities are essential for long-term growth, but you hardly need reminding in today’s market they’re not that reliable in the short run. Bonds

will never run the table in performance, at least not when high-quality corporates are yielding around 5.5%, as they are today. So think of the fixed-income funds in our simple portfolio as ballast to make your nest egg more stable.

Over the past five years, a portfolio consisting of 80% blue-chip stocks and

VANGUARD TOTAL BOND MARKET INDEX

	FUND	CATEGORY
5 YEAR RETURN	4.4%	3.8%
10 YEAR RETURN	5.7%	5.0%
ANNUAL EXPENSES	0.2%	1.0%

NOTE: Returns are annualized.
SOURCE: Morningstar.

20% bonds delivered nearly 90% of the returns of an all-stock portfolio, but with just four-fifths of the risk. Focus on high-quality bonds, which tend to zig when stocks zag; they’ve returned nearly 7% a year since 1998, beating stocks in a tough market. As you get closer to retirement, you’ll also appreciate the reliable income these bonds pay out. Today you can own the fixed-income universe in one fund, Vanguard Total Bond Market. Since bond funds return less than stock funds, low annual fees are crucial, and in this one they total just 0.19% vs. 1.02% for the average fund. That advantage makes Vanguard’s index fund very tough to beat.

ALTERNATIVES **Vanguard Total Bond Market ETF (BND)** and **Harbor Bond (HABDX)**

6 AN INFLATION-PROTECTED BOND FUND

FIRST CHOICE **VANGUARD INFLATION-PROTECTED SECURITIES FUND (VIPSX)**

FOR THE BETTER PART OF two decades, inflation has been the polio of the American economy: a terrifying danger, to be sure, but one you could confidently say was eradicated. No longer. Since last fall, consumer prices have been more than 4% higher than the year before—a rate we have not seen in nearly 20 years. Why worry if you have an ample dose of stocks? Because as you get older, you’ll gradually reduce your equity stake while boosting your bond allocation, to reflect your greater income needs and the fact that you can’t afford to take as much short-term risk as you once could. But inflation

VANGUARD INFLATION-PROTECTED SECURITIES FUND

	FUND	CATEGORY
5 YEAR RETURN	6.6%	5.7%
10 YEAR RETURN	N.A.	6.8%
ANNUAL EXPENSES	0.2%	0.9%

NOTE: Returns are annualized.
SOURCE: Morningstar.

eats away more than half of the return of a conventional bond. Enter funds made up of inflation-protected bonds. These portfolios invest in Treasury Inflation-Protected

7 A MONEY-MARKET FUND

FIRST CHOICE **FIDELITY CASH RESERVES (FDRXX)**

A MONEY-MARKET FUND is essentially a cash account. And as we’ve said in the past, cash is not an investment—it’s a place to stash your emergency fund or safeguard money you’ll need to spend right away. In fact, over the past decade, the 100 largest money funds returned just 3.6% a year on

average, barely keeping pace with the long-term rate of inflation. So why, then, include it in the only seven investments you need? As an investor, there are times when you’ll need to have some cash to manage your portfolio. What if you wanted to take advantage of a buying opportunity in the stock market, for instance? Without some money that’s easy to get at, you’d have to sell some stock or bond holdings, possibly triggering taxes. As you get older, you’ll also need an account to safely park the income thrown off by your stocks and bonds. While they don’t carry FDIC insurance, money funds are a solid choice. They’re about as safe as a bank account, since they aim to maintain principal value. Yet they’re more liquid than CDs.

FIDELITY CASH RESERVES

	FUND	CATEGORY
5 YEAR RETURN	3.1%	2.7%
10 YEAR RETURN	3.6%	3.3%
ANNUAL EXPENSES	0.4%	0.6%

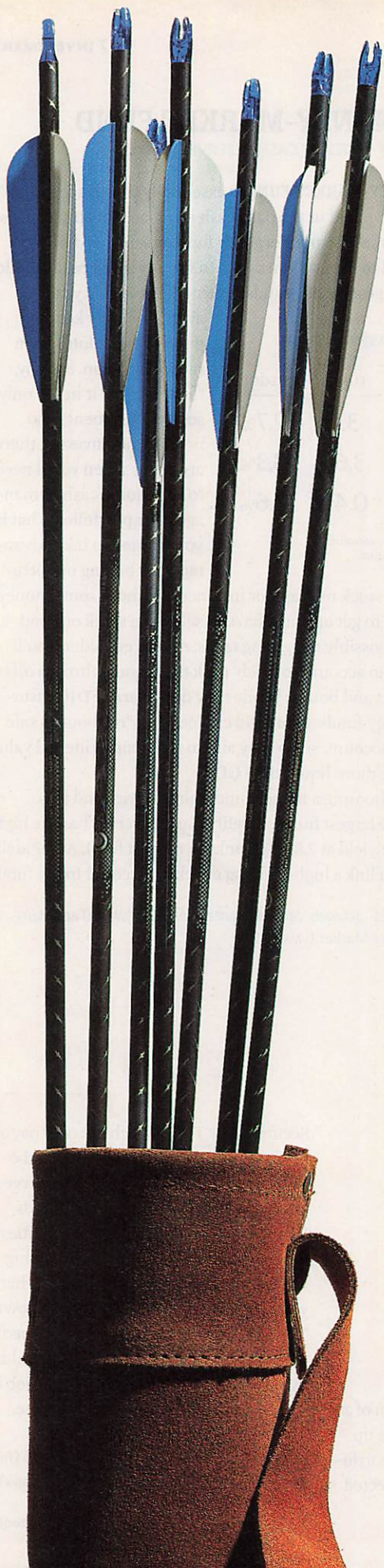
NOTE: Returns are annualized.
SOURCE: Morningstar.

When choosing a money fund, think service and fees. Among the largest funds, Fidelity Cash Reserves has the highest current yield at 2.85% (thanks to modest fees). And Fidelity will let you link a high-yielding checking account to the fund.

ALTERNATIVES **Schwab Value Advantage Money (SWVXX)** and **Vanguard Prime Money Market (VMMXX)**

Securities, or TIPS, which not only pay a predetermined yield but also adjust the value of the bond’s principal to preserve purchasing power. Among TIPS funds, Vanguard Inflation-Protected Securities has several things going for it, including lower costs and better management than you would get if you assembled your own TIPS portfolio. While the fund returned 6.6% over the past five years, you shouldn’t expect it to make a pile of dough. Its job is to protect the money you already have.

ALTERNATIVES **iShares Lehman TIPS Bond (TIP)** and **T. Rowe Price Infl.-Protected Bond (PRIPX)**



...And Where You Need to Hold 'Em

You need only seven investments for a complete portfolio, but your job isn't over once you've picked them. You must decide how much of your money to put in each. That's called asset allocation, for which you should refer to the pie charts at far right. Then comes asset *location*—the art of holding investments in accounts where the IRS can do the least damage to them. It might not matter to your overall investment strategy whether part of your portfolio is in a 401(k) and another is in a brokerage account. But it will matter to the tax man.

WHAT TO HOLD IN YOUR 401(k)

➤ **YOU'VE READ IT** in these pages, oh, at least a thousand times: The first dollars you save should be plowed into your tax-deferred 401(k). This is especially true if your employer matches your savings, which means the boss pays you for doing what you need to do anyway—save. But which of your funds belongs in your 401(k)? It depends where you are as an investor.

JUST GETTING STARTED? Then you're probably doing most or all of your investing through your 401(k). In that case, take the easy way: Build your seven-fund plan entirely within your employer-sponsored account. If your 401(k) plan doesn't offer all of the seven funds on our list (many plans have limited offerings), don't worry. The vast majority offer some blue-chip U.S. stock, foreign stock and high-quality bond funds, and many also offer small-stock and value options.

FURTHER ALONG? Once you start to acquire investments outside of your retirement plan too—in a regular brokerage account, for example—you need to pay closer attention. Inside your 401(k), priority seating goes to the funds subject to the highest taxes—namely, your taxable bond funds; they throw off interest that, outside a retirement plan, would be taxed as ordinary income.

Outside your 401(k), consider funds least likely to interest the IRS: those that generate little taxable income or whose distributions receive beneficial tax treatment. Generally speaking, this means your stock funds. This is certainly true of the equity portfolios among our top picks. They rarely generate taxable income. But when they do, much of it is in the form of either long-term capital gains or qualified dividend income. Both are taxed at a comparatively gentle maximum rate of 15%.

WHAT TO HOLD IN AN IRA

➤ **AFTER A 401(k)** with a company match, the next friendliest place for your savings is an IRA. The Roth version is particularly intriguing if you qualify (for you to contribute, your income must be below certain limits). In this type of IRA, you get no deduction for what you put in; however, money inside the Roth is allowed to grow untaxed and, unlike money in a regular IRA, also escapes taxation when you withdraw it. (In a regular IRA or 401(k), you generally owe taxes on the cash you pull out.) The Roth is appealing if you think tax rates will rise in the future—not an unreasonable bet.

WHICH FUNDS BELONG IN AN IRA? As with a 401(k), your IRA should give priority to the bonds in your portfolio, and for the

same reason: Outside a retirement account they'd be taxed much harder than your stock funds. It's especially important to shelter your inflation-adjusted bond funds, or TIPS funds, from the tax man. The principal value of these bonds rises to keep pace with inflation. Although you don't get the full benefit of these inflation adjustments until the bond matures or is sold, the IRS regards them as regular interest income and taxes you each year. That is, unless your fund is protected in an IRA. A 401(k), of course, would offer comparable tax shelter, but as of now fewer than one in eight offer such a fund. So if you're going to make a TIPS fund part of your simple portfolio—and you should—you'll want to make sure you buy it in your IRA.

WHAT TO OWN IN YOUR BROKERAGE ACCOUNT

➤ **SINCE YOU CAN SAVE ONLY SO MUCH EACH YEAR** in 401(k)s and IRAs, you probably already own some funds in a regular taxable account at your brokerage or mutual fund family. There's no hiding from Uncle Sam in these funds. Still, there are some advantages: If a fund drops below your purchase price, you can "harvest" the loss by selling shares and, at tax time, netting the loss against an otherwise taxable gain. You can't do that in an IRA or a 401(k). Plus, long-term gains and qualified dividends enjoy the reduced 15% tax rate; in a traditional 401(k) or IRA, every dollar of income—gains and dividends included—is subject to your full ordinary income tax rate when you withdraw it.

WHICH FUNDS BELONG HERE? Your taxable accounts should be the home for the stock fund portion of your simple portfolio. Don't hold any bond funds here unless your plan requires you to have more money in bonds than you can shelter in your IRAs or 401(k)s.

LOCATION, LOCATION, LOCATION

The key to the art of asset location is this: Keep bond funds in your tax-deferred retirement accounts, where the tax man can't get at them each year. The hypothetical tax-wise investor below does that. His annual tax bill is a fraction of his tax-dumb counterpart's, and after 10 years his initial \$1 million portfolio is worth an extra \$200K.

Tax-wise
Hold bond funds in a 401(k), stock-index funds in a taxable brokerage.



↓ \$1,875

\$1.7
MILLION

**AMOUNT
LOST TO TAXES
ANNUALLY**



↓ \$8,750

\$1.5
MILLION

Tax-dumb
The reverse: Hold bond funds in a taxable account, stock-index funds in a 401(k).

**ACCOUNT
VALUE AFTER
10 YEARS**

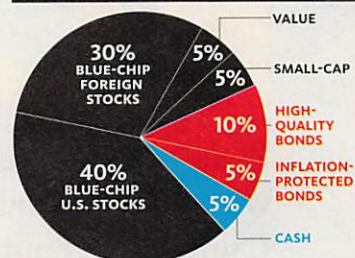
NOTES: Based on 50% stock/50% bond portfolio; assumes 35% marginal tax rate. **SOURCE:** Vanguard.

FEEDBACK: money_letters@money.com

3 SIMPLE PLANS

As you get closer to retirement, shift your money among your seven funds to create a more conservative portfolio.

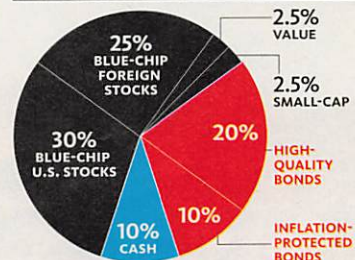
Early to mid-career



PORTFOLIO PERFORMANCE

14.3%	-21.6%
5-YEAR ANNUAL RETURN	WORST 12 MONTHS
38.7%	0.22%
BEST 12 MONTHS	AVG. ANNUAL EXPENSES

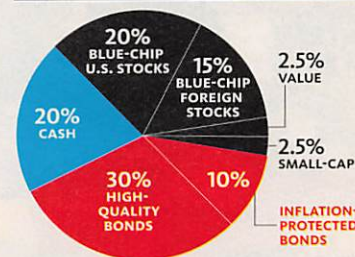
Late career



PORTFOLIO PERFORMANCE

12.1%	-14.4%
5-YEAR ANNUAL RETURN	WORST 12 MONTHS
29.8%	0.23%
BEST 12 MONTHS	AVG. ANNUAL EXPENSES

In retirement



PORTFOLIO PERFORMANCE

9.3%	-6.7%
5-YEAR ANNUAL RETURN	WORST 12 MONTHS
20.6%	0.25%
BEST 12 MONTHS	AVG. ANNUAL EXPENSES

NOTE: Portfolio figures are based on the "first choice" funds listed in the story. **SOURCE:** Morningstar.

POSTCARDS FROM THE EDGE

People in L.A. are coping in ways they never imagined with a housing bust they never saw coming. Like it or not, California's reputation as a national trendsetter is going to remain intact.

BY PAT REGNIER

PHOTOGRAPHS BY MISHA GRAVENOR





← **Hard times
hit the ranch**

Prices in sought-after Ladera Ranch, at left, took off during the boom. But they're collapsing in the bust.

↓ **But not
everyone suffers**

The Fishers pay just \$2,800 a month to live in a five-bedroom house on the water in Huntington Beach while the owner tries to sell the place.

Spring in southern Orange County has come on spectacularly. The autumn fires that blew smoke and ash into neighborhoods here also destroyed a lot of dark-hued scrub and chaparral. Now the hills along the 241 tollway are painted in bright green grasses and yellow and violet wild-

flowers. Near the end of the 241 lies Ladera Ranch, a nine-year-old (and still growing) planned community of 25,000. Nestled into the foothills, the place is a visual metaphor for the American dream, California division, in which the residents of the postmodern townhouses at the lower elevations aspire to the gated \$4 million spreads at the top. Yet there's a whiff in the air—not of smoke—but of despondency. According to Foreclosure Radar, a Web service that searches public records, more than 100 homes in Ladera Ranch are in “pre-foreclosure,” which starts when a bank sends the homeowner a first notice of default. Another 100 are in the hands of the lender or being sold at auction. So many distressed properties translate into fast-falling prices, and an owner trying to sell has a rough go of it when banks are the competition. Climbing that hill is looking harder and harder to do.

There are a lot of Laderas, and far worse, all over greater Los Angeles today. Median prices in the metro

“Everyone just kept moving.” As homes appreciated at double-digit rates, you could squeeze a lifetime of social mobility into a few years.

area's five counties are down 18% to 28% for the 12 months ended in March, according to DataQuick Information Systems, making Southern California a particularly lousy place to be selling a home right now. But the pain here isn't hard to find elsewhere. The past year has given the lie to the old saw about there being no national real estate market. Of the country's top 100 markets, 56 saw price declines; foreclosures increased in 98 of them. The same mix of crazy loans and speculative frenzy that pushed up and then pulled down L.A. was at work in Florida, the Southwest and much of the Northeast. The Midwest inflated less but in the end still proved vulnerable to a weakening economy and the debased lending standards of the bubble era.

The L.A. story, in other words, is likely to be your story too. Unlike some famous bubble towns—hello, Las Vegas—L.A. has a mature economy and a diverse housing supply. There's a house and a neighborhood like yours here, whether you live in a city, a leafy older

suburb or a brand-new exurb. In MONEY's annual special report on real estate, you'll see how homeowners in the greater L.A. area are coping and how the drama might play out here and in your hometown too. For the details on your market, turn to the forecast tables beginning on page 92. We'll also answer some key questions for buyers and sellers in a game where none of the rules are the same as they were just two years ago, and we'll look at five big changes in real estate that will outlive the crash.

First, however, the big question: When will the hurt stop? Judging from what's going on in Southern California, it's likely to be years, not months, before real estate blooms back to life.

The house you can't get out of

■ ■ To feel the pain of foreclosure, you needn't have borrowed foolishly or suffered a big financial setback. You just have to live near people who did.

“We thought we'd be able to sell pretty quickly because this is a sought-after area,” says Stuart Manley, a Ladera Ranch resident who had hoped to unload his townhouse for about \$469,000. “But shortly after we went on the market, it was foreclosure, foreclosure, foreclosure.”

Manley and his wife Judy moved to Ladera Ranch in early 2006, paying \$350,000 for their neighborhood's model home. It was a heady time to live there.

“The natural progression was that renters move up to ownership of a condo, then up to a house and then up to a mansion,” says Manley, who owns a wireless services company. In the southern O.C., where home prices were appreciating at double-digit percentages each year, you could hope to squeeze a lifetime of social mobility into just a few years. Get a loan with a low teaser rate on the first house, sell at a profit and use your new equity and another round of easy credit

to get a grander house. Patti Arnold, who handles house closings as an Orange County escrow officer, says many of those loans had minuscule initial payments, allowing borrowers to put off paying back principal. “Everyone just kept moving,” recalls Ladera resident Darlene Kelly,



FORECLOSURE BLUES

The large number of distressed properties in Ladera Ranch is making it hard for Judy and Stuart Manley to sell their place and move up to a bigger house.



speaking on the front porch of the foreclosed home where her husband, a broker, is hosting an open house.

Now few people or properties are moving up. The Manleys, for example, can afford to snap up a house that was out of their reach just a year ago—if only they could get out of their current place. (With a baby on the way, they need more room.) But there are homes nearby listing for more than \$80,000 below their asking price. Manley won't slash his price, he says, "out of respect for the neighborhood." So they're resorting to an unusual tack: trying to buy a distressed property and renting their place back to the owners. "We've had people approach us to say they're in foreclosure and need to rent," says Manley. "And I've said,



STICKING IT OUT

Scott and Joyce Porter would like to sell their Los Angeles home and downsize, but they're unwilling to cut their asking price.

"Oh, yeah, what's your address?" Meanwhile, the wave of foreclosures is changing the neighborhood, and not for the better. Manley complains about the signs that go up outside bank-owned houses on the auction block. "It feels trashy," he says.

Pay my price or I'm not selling

■ ■ Bubbles, whether they're in stocks or houses, don't explode so much as they start leaking from pinholes. The air near the edge of the bubble that props up Pets.com dissipates first. Microsoft, meanwhile, won't collapse, but it will weaken too. In real estate, new neighborhoods built farther out from town are especially vulnerable because no one's had 20 years to

build up equity. In more established areas, people who resisted the urge to treat their home like a piggy bank experience only paper losses and can, for the most part, sit tight. This is what economists mean when they say home prices are "sticky"—people just stop selling as prices drop, which slows the rate of decline. Of course, the downside to sticky is, well, you're stuck.

Scott and Joyce Porter, a semiretired couple in their seventies, put their house in the San Fernando Valley on the market six months ago for \$979,000. Scott and his now-deceased first wife bought the place in 1981. Near the height of the market, it appraised at \$1.2 million. It's a unique house that might turn off buyers reared on HGTV—no granite in the kitchen!—but it has charm to spare and a big, landscaped yard shaded by sequoia trees. "People love it," says Joyce. "It's a prime piece of property."

Apparently not at their asking price, at least not now. The Porters want to sell because it's getting harder for them to maintain so much space. Their aging Doberman struggles with the stairs.

Rather than drop the price though, the Porters have decided to take the home off the market and renovate. It's a gamble: Home values could drop while they get the work done, meaning they would have sunk more money into a place where they no longer want to be and would make even less if they did sell. Now that's stuck.



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Vehicle shown with available equipment. © 2008 Toyota Motor Sales, U.S.A., Inc.



Walking away from a bad deal

■ ■ The Porters' gamble, comparatively speaking, is a modest one when looked at against all the horrendously bad bets buyers and lenders made near the top of the market. You know the story. Wall Street figured out how to pool home mortgages into complex securities that promised investors safety even though they were backed by risky loans. That made it easy—and profitable—for mortgage lenders to hand credit to just about anyone with a signature and to give those with good credit ridiculously accommodating terms. People took on huge mortgages with little money down or with low payment rates set to explode upward in a few years. It seemed okay because rising values would make selling at a profit or refinancing a simple matter.

That's the bet Michele Porter (no relation to Scott and Joyce) made—and lost. In 2007 she bought a one-bedroom condo in Long Beach, just south of L.A., for \$289,000. Condos, not just in California but in other hot areas like Florida or the Southwest, can get especially overinflated during booms because their relatively low price draws in small-time speculators. They also attract first-time buyers like Porter who probably should have kept renting. Using a high-rate loan “piggybacked” with a smaller, even higher-rate loan, she put down only \$2,000. Her \$2,200 monthly payment was a stretch, but she was nearing 30, had landed a job scouting restaurant locations for a national chain and wanted to establish herself financially by owning a home. “Being in that rush to get somewhere, I lost clarity,” she admits.

Soon after she closed, she discovered that the apartment had a problem—the creepy, crawly kind. “Some people are afraid of heights,” says Porter. “I’m afraid of roaches.” Exterminators got rid of the bugs, but she’s too uncomfortable to live there now. Porter found a renter for \$1,100 a month, exactly half her mortgage. She’d love to sell and move on, but when she listed the apartment for \$199,000—a 31% loss—she got not even a nibble.

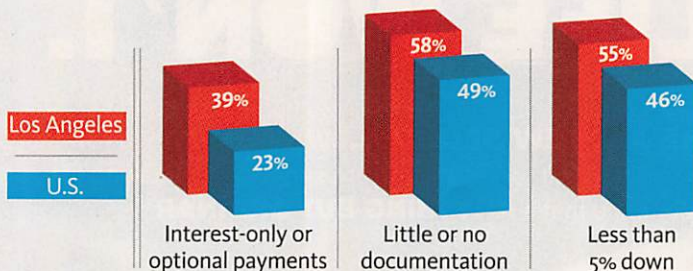
Until the market turns, Porter is in a bind, but she’s determined to avoid foreclosure and protect her credit. For more and more homeowners, though, walking away is going to look like the best of a bad set of options. Others will simply have no choice. The problem goes beyond subprime borrowers hit with rate-reset shocks. As interest rates fall, that’s less of an issue. But then there’s that class of debt known as optional-payment loans—pay the low, low minimum and the amount you owed the bank actually went up. That gimmick, pushed hard by mortgage brokers and poorly understood by many of their clients, helped lots of prime borrowers in Orange County trade up. As those loans reset, they

CALIFORNIA SCREAMING

The housing crash has hit the Los Angeles area particularly hard. But much of the rest of the country took the same reckless joyride.

1 Start with lots of funky loans

SHARE OF 2006 HOME LOANS WITH...



2 When loans blow up, foreclosures start

2007 INCREASE IN FORECLOSURES



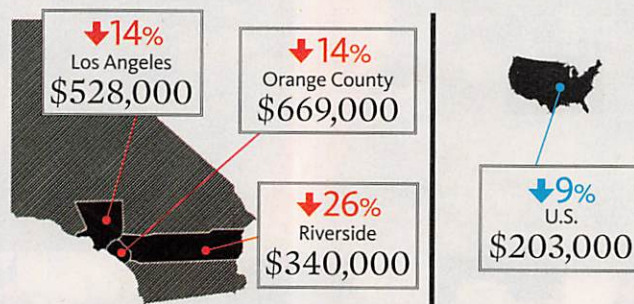
3 Foreclosures and distressed sellers flood the housing market

MONTHS' SUPPLY OF HOMES FOR SALE



4 That glut—plus tighter credit conditions—forces everyone to cut prices

2007 CHANGE IN MEDIAN PRICES



NOTE: Months' supply is for existing homes based on current sales pace. **SOURCES:** Credit Suisse analysis of loan-performance data; SMR Research; FirstAmerican Core Logic; California Association of Realtors; National Association of Realtors; Fiserv Lending Solutions.

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will be delivering payment shocks well past 2010.

The risk is that the unwinding of all this funky debt could send home prices into a downward spiral. As resets and reality force more foreclosures, putting more homes on the market, that could yank prices even lower. Those lower prices could in turn generate more foreclosures, and so on. "To some extent, it's rational behavior by borrowers to fight harder to save houses with a lot of equity than those where they owe more than it's worth," says Kurt Eggert, a law professor at Orange County's Chapman University who has studied the mortgage industry. Every month that prices slip, more homeowners lose hope.

So many homes, so few buyers

■ ■ Most people think California's real estate woes began when prices started racing southward last year. But that depends on where you stood. For home

buyers and would-be buyers who kept their heads, 2005 and 2006 were the real drag. In 2001 if the median homeowners in L.A. County bought the median home, they would have used a little over 30% of their gross income with a standard mortgage, notes Christopher Thornberg of Beacon Economics, an early and outspoken bubble basher. By 2006 that household would have used 68% of their income. "You can't do that," says Thornberg. "You have to buy food and gas and save for the future."

Let's say you wanted to live in the Santa Clarita Valley, 35 miles north of downtown L.A. In 2006 you'd have needed over \$500,000 to get a new three-bedroom starter home in Canterbury, a little pocket of houses overlooking a dry flood basin. For that price you would have gotten a community pool and clubhouse but also a steep bill to pay off a bond for schools. And your kids would be dodging cars because the lots are too small for real front yards or a sidewalk.

In 2008, Canterbury looks like a far better deal—much to the grief of those who already live here. There are 13 bank-owned or at-auction properties in the 164-home tract. "Everybody I know has no equity in

their home," says a resident who doesn't want to be identified. He bought two houses on the same street, one for about \$500,000, the other for almost \$600,000. Nearby homes are now selling in the high \$300,000s. As he stands on his porch, a Volkswagen cruises by, the driver and passengers peering out at each FOR SALE sign. "Those are the second people I've seen today," he

says. Indeed, Canterbury is crawling with real estate agents leading bargain hunters around.

At some point those discount shoppers will save the day. But too few of them are committing now, and there's not nearly enough of them to absorb the supply. Foreclosures keep flooding the market: Recently repossessed homes were one out of three sales in greater L.A. in March, according to DataQuick. But there's more to the overhang. Parts of Southern California were seriously overbuilt at the tail end of the boom as builders rushed to take advantage of high prices. And some of those projects are just finishing up now.

Like city living? Downtown L.A. is filled with condo towers in progress. Willing to take a long commute to the exurbs? Out east in Fontana, real estate agent Adam De Corte points to a listing for a group of brand-new homes for around \$388,000—just \$38,000 more than the empty bank-owned house he's showing, which after 157 days on the market is filling up with



WHAT CRISIS?

Laura and Jim Fisher decided home prices were too crazy years ago. They've figured out how to live large without owning.





Rev. Al Sharpton and Rev. Pat Robertson, Virginia Beach, VA.

It's American to disagree. It's also American to come together in the face of a challenge. And few challenges are as serious as global climate change. Take one minute to join us at wecansolveit.org and add your voice to millions of others. Together we can solve the climate crisis.

Join **we** today.

windblown grit that gets in under the doors. (On a trip out to those houses, De Corte gets lost; the streets are so new that they don't show up on his car's navigation system.) In this environment, builders who used to charge for additional electrical outlets will agree to just about anything. Want a free interior remodel? Sold.

Trouble is, to get these deals you have to 1) be able to get out of your current house and 2) get a loan. Both are tall orders right now. Keith Myers, who runs a large ReMax agency in the San Fernando Valley, says that a third of his sales now fall apart after going into escrow.

Cheaper but not cheap enough

■ ■ There are people out there who managed to resist the siren call of easy loans. They'd be ideal buyers. Matt Conrad and his wife Alison rent a three-bedroom in Mission Viejo, just outside Ladera Ranch. They considered buying a couple of years ago but decided to wait the market out after they saw that the only single-family house in their area under \$600,000 was a 1970s fixer-upper. Now Conrad, a C.P.A., checks online-discount brokerage Redfin every day for bargains. But unfortunately for the sellers in Ladera, the Conrads are in no rush despite price declines. "I'd still be paying a third more than my rent to live in a similar house," Conrad notes.

Today fewer than 10% of homes in L.A. are affordable to a typical family using a fixed-rate mortgage,

"How will you know it's okay to get back in? Simple. When prices stop falling for six months."

according to the National Association of Home Builders. Nationally, the number is 46%, down from 64% a decade ago. And around big cities with decent economies, numbers in the teens and twenties are common.

To pull the Conrads and others like them off the fence, prices are going to have to get a lot lower. So why aren't they there yet? Agents all over Southern California say that owners (like the Porters), as well as lenders with houses to sell have been slow to accept just how weak the market has become. (Agents, of course, are very anxious to record some sales ASAP.) Erik van Joosten, market manager for Redfin, observes that around 25% of listings in Orange County are would-be short sales—that is, the owner hopes to convince the bank to take a price less than the value of the loan as an alternative to foreclosure. But short sales

make up just 5% of sales pending, which suggests that banks aren't approving a lot of offers.

Maybe the banks have reason to believe things aren't as bad as they look—or maybe they're just overwhelmed by all their exploding loans. Nick Roshdieh, an Orange County agent specializing in short sales, says it can take up to 45 days for the bank even to assign a negotiator.

Adding to the confusion, for now, is the argument over a Washington bailout. Congressional Democrats, as well as presidential contenders Hillary Clinton and Barack Obama, say the only way to prevent economic crisis is for the government to guarantee some loans if banks agree to reduce what's owed. The White House and Treasury Secretary Henry Paulson have preferred a bully-pulpit approach, urging banks to work with borrowers voluntarily. That's complicated: Because of the way mortgages were sliced up and resold, the "lender" is now a group of investors with sometimes-competing interests, says Eggert. Some are first in line to get paid back and would benefit from a quick foreclosure and sale; others farther back in the queue might prefer to modify the loan. As long as the debate rages on, bankers and prospective sellers alike have a little extra incentive to hold out in hope of a better deal around the corner.

The point is that the real estate market is murky, not liquid and fast-moving like, for example, the S&P 500. It will be hard to spot the bottom when you get there. "People ask me how they'll know when it's okay to get back in," says Thornberg. "Simple. When prices stop falling for six months."

For all the anxiety and analyst sessions that falling prices have induced around L.A., a few folks have figured out how to play the game and keep winning. Jim Fisher is one of them. He lived the California dream in the bubble, and he's still enjoying it in the crash. Fisher, a software salesman, and his family are ensconced in a 5,000-square-foot home in Huntington Beach with a harbor for their backyard. And they pay just \$2,800 a month.

How? They're house-sitting while the owner tries to sell. They stage the house with their own furniture—agents believe it's harder to sell an empty house—and agree to skedaddle on short notice once there's a sale. (You want to say "Only in California," but Showhomes, the company that arranges this, is based in Nashville.) The Fishers have been roaming from mansion to mansion since 2004, when he decided that home prices were just too crazy. It sounds like an amazing deal until you see how clean they have to keep the place.

Still, there are perks. Standing in a great room that could hold Michele Porter's condo and then some, Fisher says, "I don't want to have a mortgage right now." He has a lot of company. **\$**

FEEDBACK: pregnier@money.com



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The 100 Biggest U.S. Markets

THE STATE OF HOME PRICES, WHAT'S IN STORE FOR THE YEAR AHEAD—AND WHEN THE WORST WILL BE OVER

↑ = BIGGEST GAINS FORECAST NATIONWIDE

↓ = 10 BIGGEST LOSSES FORECAST

METRO AREA	MEDIAN HOME PRICE (THOUSANDS)	MEDIAN MORTGAGE PAYMENT (% OF INCOME)	CHANGE IN HOME PRICES		***** FORECAST CHANGE TO MAY 2009	BEAR MARKET OUTLOOK			CHANGE IN FORECLOSURE RATE (PAST YEAR)
			ONE YEAR	FIVE YEARS		WHEN PRICES PEAKED	WHEN THEY'LL HIT BOTTOM	% DROP FROM PEAK	
SOUTH									
Atlanta	\$205	17%	-1.0%	16.0%	-2.3%	Q1 '07	Q2 '09	-4.4%	52%
Baltimore	264	20	-3.1	64.7	-12.5	Q1 '07	Q1 '10	-19.4	92
↑ Baton Rouge	170	17	5.7	38.3	1.9	—	—	—	14
Bethesda, Md.	460	26	-4.9	54.9	-12.9	Q2 '06	Q1 '10	-23.0	118
↑ Birmingham	156	16	2.9	29.4	2.7	—	—	—	20
Charlotte, N.C.	205	19	6.1	27.8	-0.5	Q2 '08	Q3 '09	-0.5	15
Columbia, S.C.	145	14	2.9	28.1	0.3	—	—	—	16
↓ Fort Lauderdale	309	30	-17.0	56.1	-22.2	Q2 '06	Q2 '10	-47.6	450
Greensboro, N.C.	151	16	3.9	17.8	0.6	—	—	—	256
Jacksonville	197	19	-7.9	47.7	-9.6	Q2 '06	Q2 '10	-23.3	130
Knoxville	144	15	3.1	35.6	-5.2	Q2 '07	Q3 '09	-7.4	39
Little Rock	128	13	3.9	28.4	0.5	—	—	—	405
Louisville	133	13	3.0	20.7	0.5	—	—	—	17
Memphis	124	13	-1.8	8.7	-1.5	Q2 '06	Q2 '09	-5.3	28
↓ Miami	329	41	-9.8	94.8	-24.9	Q4 '06	Q2 '10	-44.3	370
Nashville	154	15	1.6	34.8	-3.3	Q2 '07	Q3 '09	-6.0	28
↑ New Orleans	158	17	1.0	43.7	2.2	—	—	—	49
↓ Orlando	245	25	-13.1	62.5	-21.0	Q2 '06	Q3 '10	-42.8	399
Raleigh/Cary, N.C.	236	19	6.0	26.4	-0.2	Q2 '08	Q2 '09	-0.2	62
Richmond	226	19	3.8	61.4	-1.8	Q1 '08	Q4 '09	-2.4	72
Sarasota	230	23	-17.7	38.0	-15.5	Q1 '06	Q4 '09	-43.6	458
↓ Tampa	200	21	-12.8	52.1	-17.1	Q2 '06	Q1 '10	-37.6	281
Virginia Beach	236	21	3.1	90.1	-7.1	Q4 '07	Q2 '10	-11.3	33
Washington, D.C.	408	25	-10.1	49.2	-13.2	Q1 '06	Q2 '10	-30.8	42
↓ West Palm Beach, Fla.	305	28	-18.7	46.1	-17.6	Q1 '06	Q4 '09	-44.5	435
MIDWEST									
Akron	143	13	-2.5	5.2	-3.8	Q1 '06	Q2 '09	-9.4	15
Chicago	279	23	-4.6	29.2	-6.8	Q1 '07	Q3 '09	-15.0	9
Cincinnati	166	15	-4.0	7.4	-4.2	Q3 '06	Q2 '09	-10.2	9
Cleveland	145	14	-6.7	1.2	-4.3	Q4 '05	Q2 '09	-14.8	11
Columbus, Ohio	155	14	-4.2	5.7	-4.4	Q2 '06	Q2 '09	-11.3	17
Dayton	125	12	-1.8	7.7	-4.4	Q1 '06	Q2 '09	-9.0	10
Detroit	120	13	-11.5	-6.3	-8.6	Q4 '05	Q3 '09	-27.8	41
Farmington Hills, Mich.	175	13	-9.4	-7.5	-5.9	Q3 '05	Q2 '09	-24.7	N.A.
Gary, Ind.	125	12	3.8	25.6	1.1	—	—	—	12
↑ Grand Rapids	124	12	-3.0	8.3	1.9	—	—	—	37
Indianapolis	114	10	1.7	12.0	1.3	—	—	—	11
Kansas City	148	13	0.8	19.4	-0.6	Q2 '07	Q3 '09	-0.8	22
Lake County, Ill.	260	18	0.9	30.4	-0.8	Q1 '08	Q3 '09	-0.9	N.A.
Milwaukee	220	19	1.5	35.7	-1.8	Q4 '07	Q4 '09	-2.7	53
Minneapolis/St. Paul	235	17	-5.2	15.9	-5.6	Q2 '06	Q3 '09	-14.7	71
Omaha	136	12	1.4	17.7	0.6	—	—	—	71
St. Louis	134	12	2.6	31.7	-0.8	Q2 '08	Q3 '09	-0.8	22
Toledo	122	12	-4.8	1.9	-4.0	Q4 '05	Q2 '09	-11.9	12
Wichita	114	11	4.2	17.8	1.5	—	—	—	9
Youngstown, Ohio	87	10	-6.4	2.8	-3.0	Q3 '06	Q2 '09	-11.8	3
United States	\$206	20%	-8.9%	32.7%	-9.7%	Q2 '06	Q2 '09	-23.5%	65%

NOTES: The 100 biggest markets determined using 2000 census figures. Price data are for single-family homes only. Median mortgage payment assumes 5.9% interest rate, 20% down payment and 30-year term. One-year returns are for calendar year 2007, five-year from Q4 2002 to Q4 2007. One-year forecast for May 2008 to May 2009. Foreclosure rate includes properties in default and those owned by the bank and is as of January 2008.

IN 75 OF THE 100 TOP U.S. CITIES, prices are expected to fall in the next 12 months; according to Fiserv Lending Solutions, many markets won't hit bottom till late 2009 or even 2010. Pity the residents of Stockton, Calif., whose homes are likely to lose more than half of their 2006 value. But if you happen to live in Texas, congratulations: The tornado passed you by.

METRO AREA	MEDIAN HOME PRICE (THOUSANDS)	MEDIAN MORTGAGE PAYMENT (% OF INCOME)	CHANGE IN HOME PRICES		***** FORECAST CHANGE TO MAY 2009	BEAR MARKET OUTLOOK			CHANGE IN FORECLOSURE RATE (PAST YEAR)
			ONE YEAR	FIVE YEARS		WHEN PRICES PEAKED	WHEN THEY'LL HIT BOTTOM	% DROP FROM PEAK	
WEST									
Albuquerque	\$174	18%	4.7%	50.7%	-10.5%	Q4 '07	Q4 '09	-12.8%	23%
Austin	186	15	8.0	28.9	-0.1	Q2 '08	Q2 '09	-0.1	-6
Bakersfield, Calif.	255	30	-21.8	73.0	-13.6	Q2 '06	Q2 '09	-41.5	391
Dallas	161	14	3.0	15.8	1.2	—	—	—	14
Denver	254	20	-4.5	4.5	-10.8	Q2 '06	Q3 '09	-18.4	23
↑ El Paso	134	21	6.9	51.9	1.8	—	—	—	32
Fort Worth/Arlington	134	13	2.9	17.4	1.4	—	—	—	16
Fresno	276	32	-16.0	62.1	-14.3	Q1 '06	Q4 '09	-36.8	285
Honolulu	625	48	4.5	95.3	-16.2	Q4 '07	Q1 '10	-24.0	129
Houston	150	15	4.8	25.1	1.2	—	—	—	11
↓ Las Vegas	277	26	-15.7	60.8	-18.3	Q1 '06	Q1 '10	-43.1	2
Los Angeles	528	53	-13.9	67.7	-16.8	Q4 '06	Q3 '09	-36.0	261
↑ McAllen, Texas	109	22	2.1	23.3	4.0	—	—	—	23
Oakland	595	41	-15.7	27.7	-11.7	Q1 '06	Q2 '09	-33.1	266
Oklahoma City	134	14	4.6	29.8	0.3	—	—	—	16
↓ Phoenix	237	23	-15.2	60.9	-18.3	Q2 '06	Q4 '09	-39.7	9
Portland, Ore.	306	27	2.2	62.3	-14.7	Q2 '07	Q2 '10	-20.7	100
↓ Riverside, Calif.	340	33	-26.3	49.9	-16.9	Q2 '06	Q2 '09	-48.2	299
Sacramento	330	28	-22.1	23.3	-8.9	Q4 '05	Q2 '09	-40.4	210
Salt Lake City	229	22	9.7	59.9	-9.8	Q4 '07	Q2 '10	-15.2	18
San Antonio	152	16	8.3	39.6	0.8	—	—	—	22
San Diego	522	43	-14.7	31.3	-9.7	Q1 '06	Q2 '09	-32.2	175
San Francisco	840	55	-1.8	40.7	-10.1	Q3 '07	Q2 '09	-17.2	175
San Jose	750	45	-4.1	38.7	-12.5	Q4 '06	Q3 '09	-20.4	347
Santa Ana, Calif.	669	48	-13.9	52.4	-15.2	Q1 '06	Q3 '09	-35.1	290
Seattle	430	32	2.3	61.9	-9.0	Q3 '07	Q2 '09	-10.8	58
↓ Stockton, Calif.	341	32	-31.9	17.8	-16.8	Q1 '06	Q2 '09	-52.5	379
Tacoma	283	26	-0.8	64.3	-13.2	Q1 '07	Q4 '09	-18.7	68
↓ Tucson	217	24	-7.6	54.5	-16.9	Q1 '06	Q1 '10	-32.4	14
Tulsa	128 ¹	14	5.0	18.8	1.4	—	—	—	5
Ventura County, Calif.	577	41	-15.7	42.7	-13.1	Q2 '06	Q2 '09	-36.5	240
NORTHEAST									
Albany, N.Y.	200	17	4.3	64.1	0.9	—	—	—	10
Allentown, Pa.	247	21	2.2	58.9	-3.3	Q2 '07	Q3 '09	-4.4	52
Boston	363	27	-2.7	13.4	-10.5	Q3 '05	Q4 '09	-20.5	57
↑ Buffalo/Niagara Falls	105	10	1.6	24.5	2.4	—	—	—	14
Cambridge, Mass.	417	27	-1.9	10.7	-8.5	Q2 '05	Q2 '09	-15.8	57
Camden, N.J.	220	16	-2.2	50.9	-14.9	Q3 '06	Q1 '10	-24.8	11
Edison, N.J.	358	24	-6.2	36.0	-15.8	Q2 '06	Q1 '10	-30.1	0
Hartford, Conn.	249	18	-0.1	29.1	-12.6	Q1 '07	Q2 '09	-20.7	51
Nassau/Suffolk, N.Y.	465	28	-5.9	40.2	-14.4	Q2 '06	Q2 '10	-26.8	N.A.
New Haven	260	20	-1.4	36.3	-14.2	Q2 '06	Q4 '09	-22.7	83
New York City	471	45	-7.1	43.5	-13.2	Q2 '06	Q4 '09	-24.2	3
Newark	419	29	-6.2	38.1	-15.4	Q3 '06	Q1 '10	-28.4	-5
Peabody, Mass.	365	27	-3.8	10.4	-8.8	Q3 '05	Q2 '09	-17.5	9 ²
Philadelphia	200	16	1.3	50.0	-11.1	Q3 '07	Q4 '09	-14.8	29
Pittsburgh	144	14	2.0	18.1	-1.3	Q1 '08	Q1 '09	-1.5	1
Poughkeepsie, N.Y.	260 ³	19	-1.8	50.8	-6.8	Q4 '06	Q4 '09	-12.3	35 ³
Providence	275	23	-3.3	32.0	-11.6	Q4 '05	Q4 '09	-20.8	107
↑ Rochester, N.Y.	121	11	3.4	20.1	2.7	—	—	—	5
↑ Scranton	128	14	7.2	41.1	2.2	—	—	—	8
Springfield, Mass.	195	18	-2.7	33.6	-9.5	Q1 '07	Q3 '09	-14.6	241
Stamford, Conn.	562	34	0.1	32.8	-13.9	Q4 '05	Q4 '09	-21.4	66
↑ Syracuse	126	12	0.8	29.5	2.6	—	—	—	27
Wilmington, Del.	259	20	-0.6	50.9	-10.3	Q1 '07	Q4 '09	-13.2	145
Worcester, Mass.	257	20	-4.9	13.5	-9.2	Q4 '05	Q2 '09	-20.8	102
United States	\$206	20%	-8.9%	32.7%	-9.7%	Q2 '06	Q2 '09	-23.5%	65%

Metro areas may include adjacent cities. N.A.: Not available. ¹Median sales price for Q4 2007. ²Figure for nearest city in Essex County. ³Refers to all of Dutchess County. SOURCES: Fiserv Lending Solutions; First American CoreLogic; LoanPerformance data; city and county assessors in McAllen, Texas, Poughkeepsie, N.Y. and Lake County, Ill.; MetroTex Association of Realtors; Scranton Board of Realtors; and Greater Tulsa Association of Realtors.



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DISCOVER
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Whether you're buying or selling, the
real estate game has changed.
To win, you've got to learn a new playbook.

BY AMANDA GENGLER

HOUSE RULES



IF YOU'RE BUYING...



RULE 1 You can't time the bottom; you can pick a great house

→ Face it: The house you buy today will more than likely be worth less next year. That could get you thinking about trying to time the bottom. Resist. It's harder to do than you think, and this is the best buyers have had it in two decades, with inventories up and mortgage rates low. Pace yourself, find the perfect place and drive a hard bargain: Ignore the seller's asking price and bid 10% below what comparable homes are selling for. If the seller balks, move on. Remember that if you're trading up, your home could sit. So sell before you buy.

RULE 2 One reason to buy now: mortgage rates

→ Homes are plentiful and will remain so, but financing will be getting more expensive. True, the Federal Reserve has slashed interest rates, but fixed mortgages don't directly follow the Fed. They reflect the bond market's expectations about inflation, which remains a concern. The 30-year, now at 6.1%, will likely reach mid-6% by December and 7% in 2009, says Celia Chen of Moody's Economy.com. That means there could be a penalty for waiting to buy even if prices fall more. Today a \$250,000 loan would set you back \$1,500 a month. At 7%, a \$1,500 payment gets you only a \$225,000 mortgage. As for variable-rate loans, the spread between conforming ARMs and fixed loans is too narrow to do you much good.

6.1%
average rate
on 30-year
mortgage

7%
forecast rate
for 2009

RULE 3 Another reason to buy: rates on big mortgages

→ Mortgages in amounts greater than \$417,000—the limit for buying by federally sponsored mortgage agencies—usually run a fifth of a percentage point above conventional products. But investors are shunning jumbos, which now average 7.2% and are unlikely to drop much this year, according to HSH Associates.

Certain jumbo borrowers could get relief, however. A new law allows Freddie Mac and Fannie Mae to buy loans as large as \$729,750 in 71 high-priced areas. So far “jumbo conforming” loans average 6.6%. The program has gotten off to a slow start; you'll need to shop around. And unless Congress acts, this bargain will disappear at year-end.

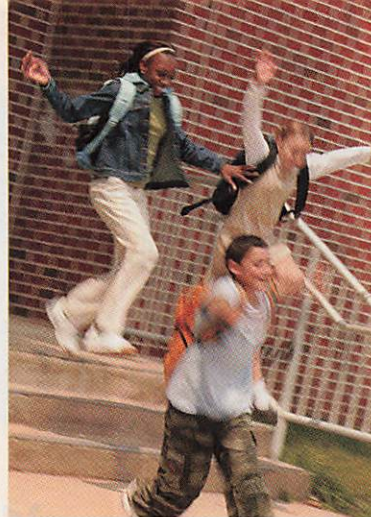
RULE 4 Don't buy cheap; buy good schools

→ By now you've heard from somebody who knows somebody who got a great deal on a foreclosed property. But when you buy a house, you're also buying into a neighborhood. And foreclosures tend to be bunched in areas where residents and speculators alike took out exotic mortgages to get into homes they subsequently found they couldn't afford. That's not a recipe for stability. Prices and quality of life could both decline further.

Similarly, avoid developments that popped up in the past few years. They too likely have a lot of owners with risky loans and little equity, says Mike Larson of Weiss Research. Instead, go for areas with highly rated schools. They generally fare better during downturns, and that pattern is holding today, according to a recent study by real estate site Trulia.com.

RULE 5 Make sure your agent has your interest at heart

→ The real estate game has a built-in conflict of interest, since the listing agent and your agent both get paid by the seller. And these days more sellers are offering extra cash to buyer's agents. So make sure you're not being steered to a house that's better for your agent than for you. Agree up front on his commission (typically 3%) and that any extra payments will go to you, says Jon Boyd, past president of a buyer's agent trade group.



IF YOU'RE SELLING...

RULE 1 Get real about price

→ Too many sellers set their price based on yesterday's market. Big mistake. "The first buyers in tend to pay the best price, so you need to price it right at the start," says Pamela Liebman, CEO of the Corcoran Group brokerage.

Have three area brokers prepare what's called a comparable market analysis. It will list asking and selling prices of similar homes, as well as amenities and sizes. If there's little inventory in your price range, list for what others are asking. If a lot of homes like yours are on the market, then look to generate buzz, says Liebman. Set an asking price 10% below what homes like yours have been selling for. That raises the odds of your getting multiple offers.

If your market is really frozen and you need to drop the price, make one large cut. No baby steps.

RULE 2 Vet your agent— especially if it's you

→ Selling on your own in an unprecedented slowdown means you'll have to work awfully hard marketing your home. If you aren't prepared for that, hire a broker. Avoid newbies. You want an agent who has been through good times and bad and who has a track record that you can verify with clients.

RULE 3 Pimp your house—hire a home stager

→ To sell today, you've got to glam up your home. A stager will help get rid of clutter (especially clutter you don't see); rearrange furniture to create attractive focal points; repurpose underused rooms, turning, say, that makeshift bedroom in the basement into a rec room; and pick paint and curtains that make rooms appear spacious. A consultation may run \$200. Completing the plan could cost \$1,000 or more. It's worth it.



RULE 4 Cash will make your home look even better

→ Given the number of listings out there, you want to throw in a little something extra to make your house catch the eye of buyers and their agents. Rather than hand out a cruise or a car—skeptics might wonder why you're so desperate—offer something that will make your home more affordable, such as paying part of the buyer's closing costs. In the multiple-listing-service description of your house that agents can see, let them know you're offering a \$1,000 bounty or a 4% commission to the one who brings in the purchaser. It will mean more knocks on your door.

RULE 5 Underwater? Learn to swim

→ If you're a recent buyer, your mortgage may well top what your home would go for today. About a third of those who bought last year or in 2006 now have negative equity, according to Zillow.com. If a job or family issue compels you to move, your options aren't great, but you have a few. First, you may be able to persuade your new employer to make you whole on the loan. Second, if the rental market in your area is strong (as is the case in many spots that were healthy but not overly bubbly during the boom), you can become a landlord and wait out the slump. Third, of course, is to sell for as much as you can (see Rule No. 1) and raid your savings for the difference.

Short sales, in which the bank agrees to take less than it's owed and release you from your debt, get a lot of media attention. That doesn't mean they're easy to come by. A bank usually will consider one only if you're at risk for foreclosure. Even then it may say, "No, thanks." \$





*Tons of natural stone!
Hand-painted walls!*

50,000 B.C.



*Unobstructed
prairie views!*

1870

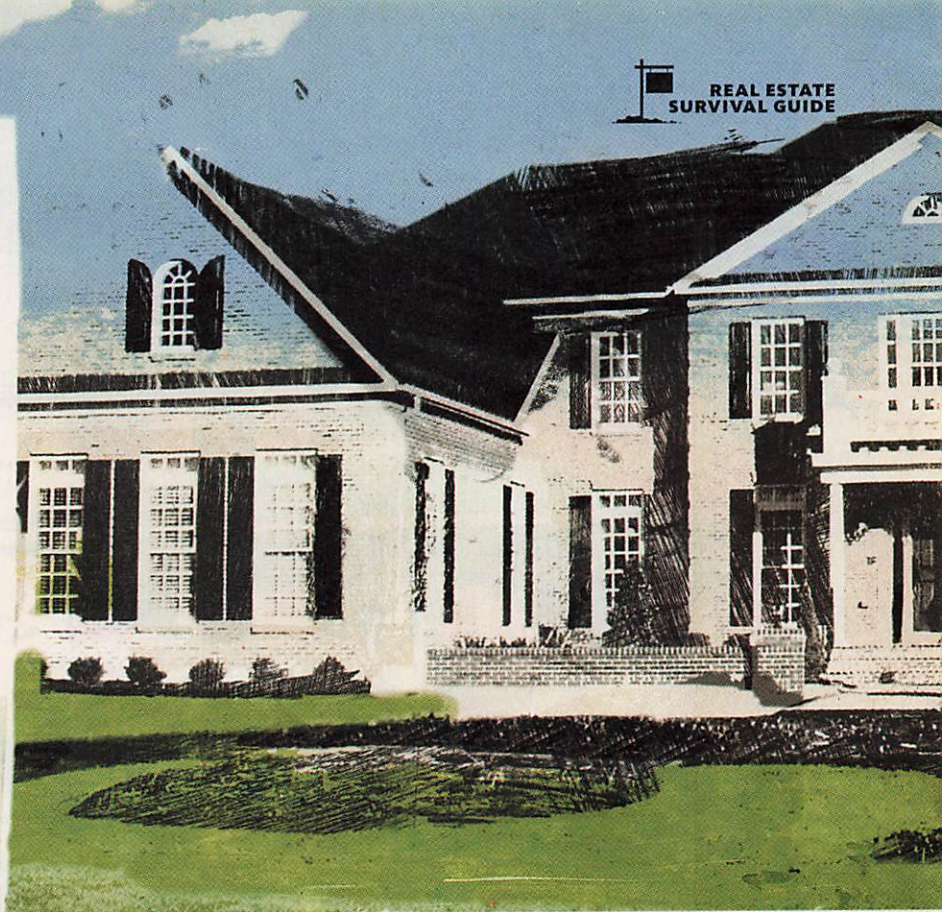
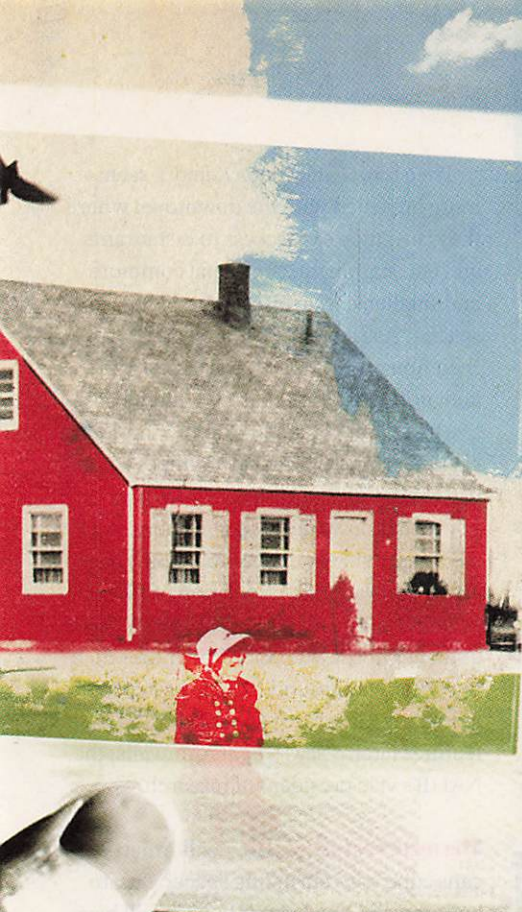


REAL ESTATE'S

Next Evolution

This post-bubble, credit-crunched market won't last forever. Coming on strong are new trends that will reshape tastes in homes and transform how you buy and sell. **Here's what lies ahead.**

BY STEPHEN GANDEL | ILLUSTRATIONS BY TOM BURNS



*Ideal for starting a
baby boom!*

1950



*More room than
you'll ever use!*

2000

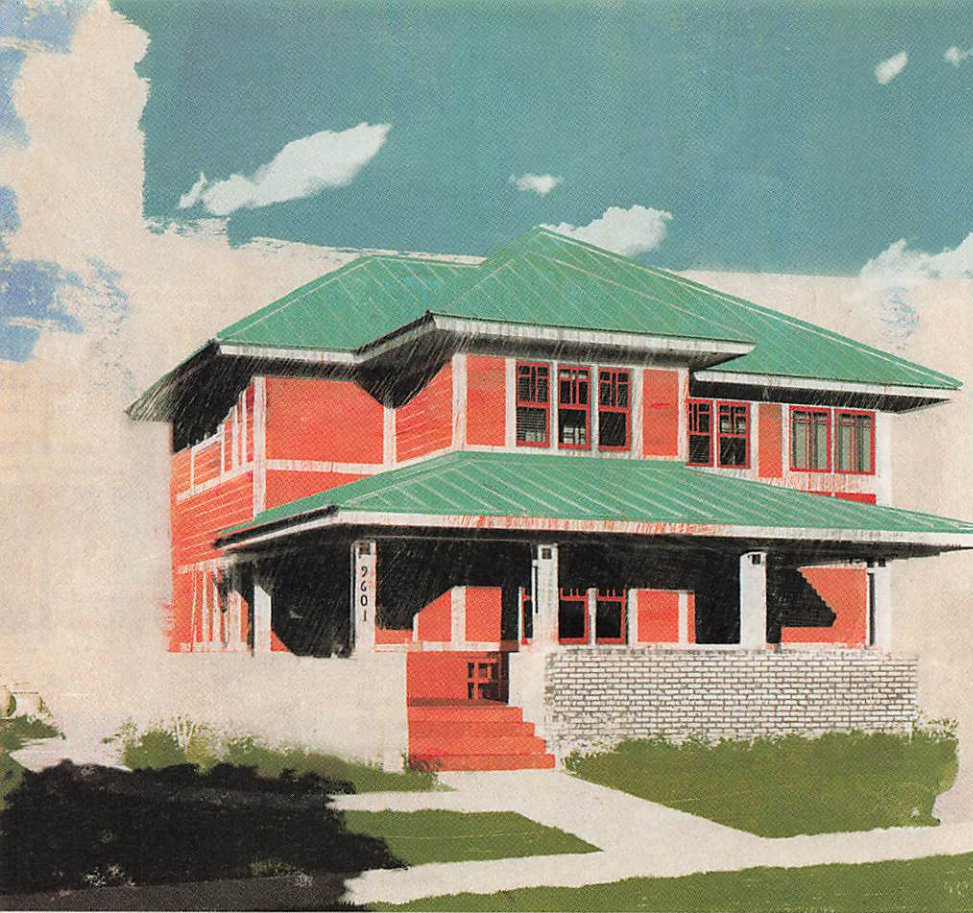


One thing, at least, is certain about real estate: At some point—not this year and maybe not next, but someday—housing prices will start to come back. Real estate values may not be where they were at the market peak in early 2006, but homes will once again look like a safe place to put your money.

Still, you shouldn't kid yourself. The real estate market will not go back to the way it was before the bubble. We have learned too much. We know now that the value of our property can fall as well as rise. We've learned through hard experience that mortgages can't be repaid with hope. And we've come to understand that real estate, like every other asset, is no guaranteed path to wealth. And maybe bankers, homeowners

and investors have realized that easy money isn't something to count on forever.

It isn't only market psychology that will change. The current credit crisis will transform how homes are sold and financed and who bears the risk. Soaring fuel costs, environmental concerns and the movement of the baby-boom generation into the ranks of the elderly will certainly alter what Americans want in a home. Online technology could democratize how we shop for property and finance it. And new investment vehicles could help cut—or increase—our risks. "All of these things will force us to reinvent how we think, build and purchase housing," says futurist Glen Hiemstra. Here's what the next stage of real estate might look like. >>



The post-McMansion McCottage

YOUR NEXT House—Smaller

» **OUT ON THE RANGE** IS the last place you would expect America's long-running obsession with big houses to be laid to rest. But four years ago Rachel Odom, an Oklahoma City home builder, began constructing an exclusive development where houses average just 1,800 square feet. That's far smaller than the homes of up to 6,000 square feet that her company had been building until then—and nearly 500 square feet smaller than the national average for new construction. "Our concept was that people would pay up for smaller homes with more architectural character," says Odom. "But since nearly everyone seems to dream of owning a large home, we were taking a huge risk." That risk may not have been as big as she thought. In Odom's Talavera development, where houses cost as much as \$275,000 (or about double the median local home price), she sold 115 homes in the first 18 months and expects to sell as many as 600 in total. These days small houses are, you know, big.

Up until now: Over the years, many a seer has predicted the mass downsizing of the American home. Instead, the average size of newly built houses has continued to rise from just over 1,600 square feet in the late 1970s to nearly 2,300 now. But a number of trends suggest that this time Americans really might be willing to swap their McMansions for McCottages. For starters, baby boomers, whose eldest members turned 62 this year, are increasingly becoming empty-nesters; with children gone, they need less space. Families themselves have changed dramatically. Between 1970 and 2000, the percentage of nuclear families—married couples with kids—declined from 40% of households to 24%, according to the Census Bureau. And childless families are expected to increase. For them, the supersize house may no longer be the ideal.

Then too, Generations X and Y seem more intrigued with life downtown where they can enjoy easy access to restaurants and entertainment, a minimal commute and smaller, easier-to-care-for living spaces. "Ask anyone how many rooms in their house they don't regularly go into and most will admit that they actually live in a small percentage of their home," says Marianne Cusato, an architect who used to design 3,000-square-foot-plus homes but now specializes in cottages. In a February survey of potential home buyers by the National Association of Home Builders, 60% said they would rather have a smaller house with more amenities than the other way around. "In the past, people would say 'Give me space and I'll add the features later,'" says Gopal Ahluwalia, the NAHB's vice president of research.

The next evolution: How will Americans cope with shrinking space? Cusato believes that newly built houses will have layouts that can "live bigger" than their square footage would suggest. Rooms can do double duty. For example, a den can be dressed up as a formal living room when needed (which Cusato contends is not that often). Also slated for possible demolition: the formal dining room. Families can satisfy all their dining and entertaining needs by slightly expanding the breakfast nook. The great room could also become a relic. "Open spaces are great, but people don't know how to use undefined rooms," says Cusato. "So they don't." Sarah Susanka, author of *The Big Little House*, agrees. "The majority of your guests want to be in rooms you live in, not have their socks knocked off by a three-story foyer." She says storage can swallow a lot of a small house as well. So she designs homes with as much built-in storage as possible.

If the trend toward smaller homes does take root, it could trigger a seismic shift in home values. A recent study by online house-pricing service Zillow.com (more about it later) found that less expensive houses appreciate more than costlier and presumably larger homes. If that continues, the ubiquitous McMansion may turn out to be the real estate bubble's biggest booby prize.

YOUR NEXT Mortgage —Risk-adjusted

>> IT'S ENTIRELY POSSIBLE that in the future buying a house that is shocking pink, ultramodern or in a neighborhood that's up and coming (no Starbucks yet) could add an extra fee to your mortgage for what banks perceive as added risk. With foreclosures projected to reach 2 million nationwide by the end of next year, bankers are rethinking how they set mortgage rates. "The industry would love to be able to do a retinal scan before they give you a mortgage," says Keith Gumbinger, vice president of HSH Associates, which tracks the home-lending market. "They want to be able to assess the risk—practically down to the biological level—that you won't pay your mortgage."

Up until now: There have always been differences in rates. But historically they were based on the type of mortgage you chose and the amount of money you borrowed. A 30-year fixed-rate mortgage, for example, would come with a higher rate than a 15-year fixed-rate loan because over 30 years there was a greater risk that interest rates would rise. What's more, mortgages for less than a specified amount (previously \$417,000 and now as much as \$750,000, depending on where you live) could be off-loaded to Fannie Mae or Freddie Mac. Because banks didn't have to bear the risk of default on mortgages sold to those government-backed insurers, they came with lower rates. But as long as your credit score was 580 or higher (on a scale of 350 to 850), the rate was the rate. "Everyone who was prime had the same rate," says Scott Happ, CEO of Mortgagebot, a lending technology company. Now that is changing.

The next evolution: Lenders have already begun to assess up-front fees that vary with credit scores. Instead of a great divide between the "have a 600 credit score or better" elite and the unlucky have-nots, there will be graduated levels of risk. Gumbinger says, for example, that borrowers with credit scores of 700 to 719

making 20% down payments can expect to pay an additional fee of as much as 0.5% of their total mortgage at closing beyond what is paid by those with a higher credit score. And if the credit score drops to between 660 and 679, the fee can more than double to 1.25%. Some lenders assess the fee by boosting their interest rates. "Credit scores matter more than they used to," says Jack Guttentag, founder of the Mortgage Professor website and professor of finance emeritus at the Wharton School. "Everything matters more than it used to."

That's just the start, however. Eventually, mortgage pricing may come to resemble pricing for, say, homeowners insurance, which takes into account dozens of factors, including your neighborhood, whether your house is brick or wood, its replace-

houses or ones in so-so neighborhoods, they could charge higher up-front fees or interest rates for those too.

The good news is that this new wrinkle could help borrowers with pristine credit records and conventional tastes get lower than average interest rates and better terms on a mortgage than they did previously. For now, credit scores matter the most, and the higher your score is, the lower your rate and fees will be. (For our tips on boosting your number, go to cnmoney.com/credittips.) But larger than normal down payments—25% to 30% of the value of the property, for example—can also lower your interest rate by convincing the bank that you won't walk away at the first sign of an economic chill.

The bad news is that even if you have a high credit score, tailored mortgage pricing could make getting a home loan more time consuming. According to a 1999 study by the Mortgage Bankers Association, many borrowers get their mortgage from the first lender they talk to, usually the one

YOUR BRAVE NEW MORTGAGE FEES

Mortgage lenders are starting to price loans the way other lenders do: charging borrowers with lower credit scores higher rates or extra fees. If your score is above 720, no problem. The more your score dips beneath that threshold, the more you'll pay in extra fees.

IF YOUR SCORE IS...

680-719

0.50%

YOU
WILL PAY
AN EXTRA
FEE OF...

660-679

1.25%

640-659

1.75%

620-639

2.50%

LESS THAN 620

2.75%

SOURCE: Freddie Mac.

ment cost, its proximity to a fire hydrant, your credit score and past insurance claims for the house before you bought it. Now mortgage bankers too may begin to include in their assessment of your riskiness the size of your down payment, your employment history, the house's history and anything else that might affect repayment of the loan. Going on the theory that only the less financially responsible would purchase shocking pink or ultramodern

recommended to them by their real estate agent. But with lenders considering factors they never did before, the result is going to be a much wider variety in the rates you are offered by different brokers and banks. (Some banks may have no problem with shocking pink.) The moral: In the future you will want to invest much more time shopping for a mortgage loan than the average person does today. The payoff for doing so is going to get a lot larger.



YOUR NEXT

Real Estate Agent — Cheaper

>> WHEN CINDY BROCKWELL, 58, and Bill Dailey, 62, sold their townhouse in Reston, Va. in early April, the only real estate agent involved was the one who brought them their buyers. Instead of a listing broker, they used Internet services including ForSaleByOwner.com to price their house and do all the other things a broker would normally do. "We decided that the value of the listing agent was minimal," says Brockwell, who found a buyer in just five weeks. The total commission came to 3%.

Up until now: You couldn't really operate in the residential real estate market without access to the National Association of Realtors' multiple-listing service. The monopoly meant that only realtors really knew what homes in your area were selling for. They'd be happy to share the data—in return for the standard 6% commission.

The next evolution: Real estate information wants to be free. An estimate for just about any home's value at any time will soon be available online at Zillow.com, HomeGain.com, RealEstateABC.com and other websites. Zillow and its ilk are not perfect. Zillow's valuation program, for example, tends to work best for mid-price homes in areas where there are a lot of transactions, less so in neighborhoods where people seldom move. But the time may come when Zillow is seen as more reliable than human brokers. Like owners, brokers get anchored to higher prices as home values fall, and they have an incentive to inflate estimates to win prospective clients. Zillow has no such biases. If your house is worth \$50,000 less than you paid a year ago, Zillow will tell you. It can't be fired.

John Vogel, who teaches economics and real estate at Dartmouth, says the democratization of data spells the end of the 6% commission. "You go to an agent for information," says Vogel. "Free access to it should be a major threat to the brokerage business." Real estate brokers will still have a role as marketers, especially in tough times like these. But like stockbrokers before them, they'll find that as they lose their traditional monopoly on information, they just can't command their traditional price.

NO MORE SECRETS

Thanks to online services, real estate information has spread from agents to customers and turned Americans into a nation of "real stalkers." With sites like Zillow.com, everyone now knows how much everyone else's house is worth.



Hill and Bill's house in Chappaqua, N.Y.



NAME	BEN BERNANKE	MARTHA STEWART	ALAN GREENSPAN	HILLARY CLINTON	LARRY KING
HOME	Washington, D.C.	Katonah, N.Y.	Washington, D.C.	Chappaqua, N.Y.	Beverly Hills
EST. VALUE	\$920K	\$1.7 MILLION	\$1.8 MILLION	\$2.2 MILLION	\$11.7 MILLION

SOURCES: Public records, Zillow.com.

YOUR NEXT

Mortgage Broker

— Not a crook

>> DAVE PRUKA, 41, a Minneapolis publishing executive, went hunting for a mortgage earlier this year but didn't bother with a broker. Instead he visited several banks and eventually a website, MortgageMarvel.com, which allowed him to see rates from dozens of lenders at once. "I didn't like the idea of having someone else do my shopping for me," says Pruka. "I wanted to ask the questions and hear multiple answers and then do the comparison myself."

Up until now: What a difference a burst bubble can make. Only two years ago, mortgage brokers originated more than two-thirds of new loans, according to Wholesale Access, a mortgage research firm. Now their share of the mortgage pie has dropped to 45%. That's a shocking loss of market share when you consider that brokers were supposedly a boon to borrowers. Because they don't work for any one bank, they can shop dozens of lenders on your behalf to get the best loan at the lowest price.

But they seldom did. Instead, brokers pocketed kickbacks from banks in return for selling borrowers unnecessarily costly loans. An April study by the Center for Responsible Lending, a nonprofit organization working to eliminate abusive lending practices, found that among borrowers with credit scores of 640 or less, those who used brokers paid an average of \$5,222 more in the first four years of their mortgage than those who borrowed directly from a bank. Borrowers with credit scores of 640 to 720 paid \$1,316 more.

The next evolution: To survive the shakeout in their industry, mortgage brokers will have to do business more transparently. A number of bills before Congress would require them to disclose fees and take on a fiduciary responsibility.



Some pieces of European design belong in a gallery. Ours work best in the kitchen.

With my new Electrolux collection of premium appliances, it's easy to keep my guests entertained. Now I know why Electrolux appliances have been used in fine European homes and restaurants for over 70 years. The full line of appliances is designed with ingenious features to help you be even more amazing, like:

Luxury-Glide™ Racks smoothly extend with the touch of a finger.

Wave-Touch™ Control Panel keeps virtually endless cooking options hidden until you need them.

Luxury-Design™ Lighting is as beautiful as it is functional.

See the full collection of Electrolux appliances and Kelly Ripa star in the "Cupcake Queen" at Lowe's.com/Electrolux

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Electrolux

ity—that is, represent their client's best interest. A few large banks are cutting mortgage bankers out of the process. Bank of America and Wachovia, for example, have recently said they will make all loans directly to customers. Several websites have arisen to facilitate such direct sales. MortgageMarvel.com, which launched in November, can get you quotes from 280 banks and credit unions around the country and, unlike Bankrate.com, Lendingtree.com and other familiar online names, does not steer you to mortgage brokers.

MORTGAGE BROKERS: NOW YOU SEE THEM...

During the bubble, brokers originated more than two-thirds of all mortgages. Now they account for fewer than half.

SHARE OF LOANS ORIGINATED BY BROKERS



NOTE: ¹Estimated. SOURCE: Wholesale Access.

If you still want help from one, you don't have to wait for the regulators, however. You can insist on reformed behavior yourself. Demand that your lending middleman set his fee in advance—not just what you will pay but also what he will get from the bank, which affects your rate. His or her total fees should not exceed 2% of the loan. A growing group, referred to as up-front brokers, make a practice of baring all for you. You can find a list of them at upfrontmortgagebrokers.org.

YOUR NEXT Real Estate Investment — Futures

>> WOULDN'T IT BE COOL to invest in a house without the pain of owning it? No painting or fixing, no worries about the tenant's furnace cutting out in the middle of the night. The means to such a pleasant end are real estate futures, co-invented by Robert Shiller, Yale economist, author of the bestseller *Irrational Exuberance* and predictor of the collapse of the recent housing bubble. Futures could offer investors a quick way to get in and out of the housing market and homeowners a way to hedge the equity in their homes. If you haven't heard of them yet, don't feel bad. "They just haven't caught on like I expected," says Shiller. That might be changing.

Up until now: For a long time, the only way to invest in residential real estate was to buy a house. You earned income if the rent you got more than covered your expenses. Then if the price went up, you pocketed the gain when you sold. That gain on selling was all anyone focused on in recent years. Of course, the opposite was true too. If prices sank, you could be stuck with a white elephant that you still had to heat and light.

HOUSES vs. HOUSING FUTURES

Futures let you invest in residential real estate without owning a house or hedging the risk you have in a house already owned. Futures have more leverage, which magnifies both gains and losses.

*Hedge your money
pit in the futures pit*



NOTE: Assumes a \$10,000 investment and a 10% down payment on the house.

The next evolution: Two years ago, the Chicago Mercantile Exchange, with the help of Shiller and others, launched housing futures, which track the S&P/Case-Shiller Home Price Indices for 10 metropolitan areas and a composite that represents the nation. The price of a housing futures contract rises and falls with the market's perception of where housing prices will be in six months or a year, depending on the date of the contract.

So far, so good. But here's why contracts make interesting hedges: To purchase one \$50,000 housing futures contract, you need invest only \$2,500. With that kind of leverage, a 5% rise in the housing price index would double your money. The same investment in a house, assuming you put 20% down, would grow by 25%. Of course, if the index were to drop 5%, your futures contract would be wiped out. Leverage cuts both ways.

Shiller predicts that the main traders of housing futures will be builders, who will sell contracts to hedge their inventory. (When you sell a contract, you make money when prices go down.) All of that business-related selling could pressure prices unrealistically. Indeed, in mid-April, futures were predicting that home prices in Los Angeles would fall 33% this year. That's nearly double the drop forecast by Fiserv Lending Solutions (see our table starting on page 92). And that, says Shiller, might just mean something you haven't seen in a while in real estate: a buying opportunity. **\$**

FEEDBACK: sgandel@money@mail.com



Project Planner

A Place for Everything

Kitchen cabinet organizers turn storage chaos into storage control.

“Where’s the potato peeler?” “Don’t we have dozens of containers for leftovers?” “Can’t find the popcorn popper!” These—and many others like them—are the kinds of complaints heard in a cluttered kitchen, where cabinets become black holes, drawers define chaos, and meal prep isn’t much fun. But there are dozens of simple solutions for this problem, all of them arrayed under a most helpful heading: kitchen cabinet organizers.

Imagine being able not only to store more stuff but also more easily find what you’re looking for. That’s what this group of gadgets will do for you, by conquering clutter and putting everything in its proper place. Your base cabinets can be upgraded with roll-out shelves, trays, bins, and dividers that will put those platters, mixing bowls, and cutting boards at your fingertips. That big hunk of storage lost in a corner cabinet can be reclaimed with a swing-out shelf that tucks away into the deepest recesses. Your trash and recycling programs can be upgraded with a large pair of pullout containers.

To sort out these and many other options, get online with Lowe’s, and you’ll be on your way to making your kitchen easier to use and yourself a happier cook. ●

DIFFICULTY: BEGINNER
TIME NEEDED: A FEW HOURS
EST. COST: \$5 TO \$60 PER CABINET ORGANIZER



The Options...

INSIDE CABINETS

For whatever you’re storing, put an end to stooping and searching with an easily installed roll-, pull-, or swing-out shelf, tray, or bin.

DRAWERS IN ORDER

Utensils and gadgets will find their proper place in drawers fitted with drop-in organizers. You’ll get instant results.

BEHIND CLOSED DOORS

To gain easy access to cleansers, cleaning tools, spices, and more, the backs of cabinet doors can be fitted with slim racks and shelves.

From Start to Finish...

1 PARE DOWN:

There may well be a fair amount of stuff that’s being stored but not being used. If it’s been a couple of years, you can probably toss it and never miss it.

2 PLAN AHEAD:

Figure out which cabinets and drawers need organizers. Usually it’s the base cabinets and wall units. Take measurements and make a list of their heights, widths, and depths.

3 SEARCH AROUND:

Go online or to the store to find out what your specific options are. Try to create uniformity by choosing devices made of similar materials.

4 DO-IT-YOURSELF:

Installation is simple, often consisting of little more than putting a few screws in the right places. Many kits have full-size templates and easy directions.

LEARN FROM THE EXPERTS WITH PRODUCT INFO AND DO-IT-YOURSELF GUIDES AT Lowes.com/HomeOrganization



How to See the Rebound Coming

Sooner or later the economy and the markets will take a decisive turn for the better. **Good things will happen to those who spot that moment first.**

BY JANICE REVELL

PHOTOGRAPHS BY
MICHAEL LLEWELLYN

→ **BY NOW YOU'VE HAD ENOUGH** of the endless gloom in today's economic news: record oil prices, slower home sales, deepening loan losses, disappointing corporate earnings. What you're really looking for at this point are a few signs of hope. It's a certainty that the economy, the housing markets and the stock market have to bounce back sooner or later. If you could see that rebound coming, not only could you rest easier about everything from your job to your retirement, you could move forward confidently on all those financial plans you've put on hold until the way seemed clear. You could, maybe, take a chance in the job market. You could think about trading up to a bigger home or downsizing to a place that better suits your needs. And even though you've stood unwavering by your investment strategy as the stock market tumbled—and you have, haven't you?—you could feel good once again about putting your money in something besides a chickenhearted money-market fund.

So what are the surefire signs that we're bouncing back? The only honest answer, of course, is that there are no 100% surefire signs. In every cycle there are wild cards that can trump even the best predictions. On the other hand, history shows that some hints of renewal are far more reliable than others. At least one of them is worth watching in every market that matters to you, from stocks to real estate to jobs. Turn the page to find out where you'll find these harbingers of economic spring, why they work and how you can make the best use of them. →



When Will the **Economy** Get Out of a Rut?

WATCH: BUSINESS SENTIMENT
CURRENT READ: RECESSION'S STILL ON

→ **WHILE WE WON'T KNOW** for certain whether we are in a recession—defined as a decline in gross domestic product for at least two quarters in a row—until later this year, most economists believe we are. For starters, GDP growth slumped to an anemic 0.6% in late 2007.

What's more, the measure that has been eerily prescient in the past decisively flashed "recession" just as the housing market peaked. We're talking about the yield curve—or the relationship between short- and long-term interest rates. Long-term bonds usually pay more than short-term ones to compensate investors for locking up their money. When that relationship flips and produces what's known as an inverted yield curve, you can be pretty sure a slump is coming.

Since 1960, every time the yield curve, as measured monthly, has inverted (except once), a recession has followed. The last time this happened was July 2006. Unfortunately, the yield curve can't

help you see the recovery that's bound to be over the horizon. What can?

WHAT TO WATCH The most important clue may lie in the minds of business leaders, says Nariman Behravesh, chief economist at Global Insight. The more upbeat companies feel about their prospects, the more likely they are to expand and hire, which in turn lifts consumer confidence, sparks spending and boosts economic growth.

To get a read on business sentiment, Behravesh suggests looking at the Institute for Supply Management's nonmanufacturing index, a monthly survey of conditions in the service sector, which accounts for 80% of jobs. A reading below 50 is typically regarded as a recession signal; the lower it goes and the longer it stays down, the more severe the slump. Once it returns to 50-plus territory, a rebound is likely.

During the brief recession of 2001, the index dropped below 50 just as the slowdown started and hovered between 45 and 50 for most of the next eight months. A month before the recession ended, the index rose sharply to just under 50

and soon stabilized in the low 50s.

FOR A SECOND OPINION Look to the real estate market. "Housing is what got us into this recession," says Gus Faucher, director of macroeconomics at Moody's Economy.com. "In terms of what's going to get us out of it, we're going to be looking for a bottom in the housing market."

How do you spot that? Brush up on supply and demand. Historically, the inventory of homes on the market—particularly how many months it would take to sell it off—has soundly predicted home prices. Six months of inventory appears to be the sweet spot. In 1996 inventory fell below six months and dropped for much of the decade—and prices climbed steadily.

WHAT THEY'RE SAYING NOW A mixed outlook. For March the ISM nonmanufacturing index stood at 49.6—up from the precipitous drop to 44.6 in January but still below 50 for the third straight month. "If the index goes to 40 and stays there, we're looking at a much deeper recession," says Behravesh. "If the number goes back up to 50 and remains at those levels, that's

When Will Inflation Cool Off? WATCH: MONEY SUPPLY / CURRENT READ: NO COOLDOWN YET

➔ **AS YOU KNOW** all too well from the skyrocketing cost of the milk you put in your cereal and the gas you pump into your car, inflation is back. Consumer prices are rising at 4% a year—well above the 2.6% average annual increase of the past decade. Predicting inflation is one of the most hotly debated areas in economics. Still, there's one signpost worth watching.

WHAT TO WATCH Follow the money supply. When the Federal Reserve cuts

rates, it often does so by buying Treasury bonds from banks, giving them more money to lend and thereby pumping more money into the economy. When the growing supply of greenbacks outstrips demand, each dollar is worth less and buys less. Presto: inflation.

Every major increase in inflation over the past century has been preceded by a spike in the money supply, and a dip in the growth of the money supply has usually led to a drop in the

inflation rate. In the early 1980s, when inflation topped 10%, then-Fed chairman Paul Volcker embarked on an aggressive campaign to slow money supply growth and tame inflation. He succeeded—by 1983, inflation was 3.2%—but at a price. Clamping down on the money supply helped trigger a severe recession—one reason today's Fed is under pressure to keep up money supply growth.

WHAT IT'S SAYING NOW Going by the money sup-

ply, odds are good that inflation will continue rising in coming months. Since last September, the Fed has been on a rate-cutting tear, slashing the federal funds rate by three percentage points in an effort to stave off recession. As a result, the money supply measure known as M2 has grown by a compound annualized 14% rate over the past two months. To put that in perspective, M2 grew at an average annual rate of 6.1% from 2000 to 2008.

TO KEEP TRACK You can look up M2 at the website of the Federal Reserve Bank of St. Louis: Research.stlouisfed.org.

THE WILD CARD It's not just the Fed that has control over our money. The owners of U.S. dollars can increasingly be found outside the U.S. China holds an estimated \$1 trillion, much of it in the form of Treasury bonds. A decision by China to liquidate even a modest portion would drive up the money supply.

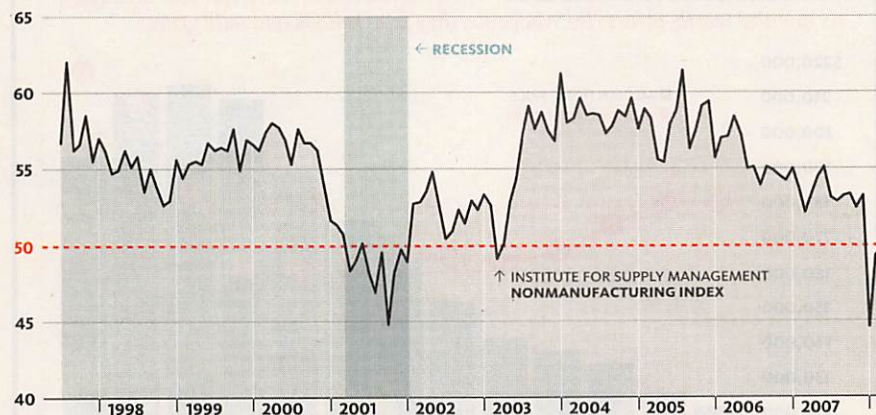
definitely a signal that things are going to get better." Housing inventory, however, has recently hit nearly 10 months' worth—bad news for prices and growth.

TO KEEP TRACK The ISM nonmanufacturing index is released on the third business day of every month. It's widely reported in the press; or you can find the releases in the ISM Report on Business section of ism.ws. As for the real estate inventory yardstick, the National Association of Realtors puts out the data monthly (usu-

ally between the 22nd and 25th). Look in the Research section at realtor.org. **THE WILD CARDS** As Federal Reserve governor Kevin Warsh recently quipped: "If you've seen one financial crisis, you've seen one financial crisis." Indeed, this slowdown has seen a massive credit crunch, a free-falling dollar and record oil prices. At the same time, exports to China and India are helping U.S. businesses offset weakness at home. Any or all of these factors could cloud the rebound picture.

Keep an Eye on the Business Mood

A shift in business sentiment can signal a recession or recovery. A sustained dip below 50 suggests a slowdown. A return to 50-plus territory is a good omen for growth.



SOURCE: Institute for Supply Management.

When Will Stocks Stop Tumbling?

WATCH: THE FED
CURRENT READ: A SUMMER RALLY

➔ **THIS SPRING** the stock market has flirted with the 20% decline that would mark an official bear. Now what every investor wants to know is when stocks will start climbing back.

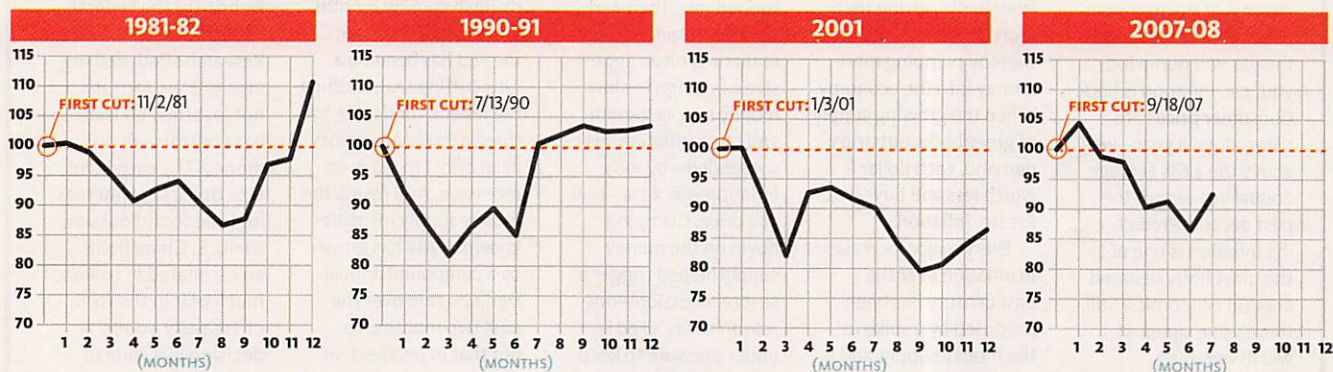
WHAT TO WATCH Again, follow the Fed. "Interest rates are probably the one thing that you really want to pay attention to," says Sam Stovall, chief investment strategist for Standard & Poor's Equity Research. Of the dozen times the Fed has embarked on a series of rate cuts since 1954, the S&P 500 has only once failed to deliver a gain one year later.

Why are rate cuts such a reliable predictor? Over the long term, stock prices follow corporate earnings, and while analysts use all sorts of methods to place a value on future earnings, one principal remains constant: The lower rates are, the more valuable future earnings are to investors.

FOR A SECOND OPINION Not convinced by the march of history? Check out stock valuations. When share prices are cheap relative to earnings, the market is poised ➔

To Call the Market, Follow the Fed A year after the Fed starts cutting rates, stocks tend to be up. That's held true during two of the past three recessions. The exception: 2001, when extraordinary world events intervened.

→ S&P 500 FOR 12 MONTHS AFTER RATE CUTS BEGIN (INDEXED TO 100)



SOURCE: Standard & Poor's.

to take off. One way to judge cheapness, says Stuart Freeman, an equity strategist at Wachovia Securities, is to compare the earnings yield of the S&P 500—the inverse of its price/earnings ratio—to the yield on government bonds. The more the S&P 500 is yielding vs. bonds, the more inexpensive it is—and the more likely a recovery is.

WHAT THEY'RE SAYING NOW Based on rate cuts, the stock market should be going on a tear any minute now. But since the Fed began to lower rates last September, the S&P 500 is down about 8%. Stovall believes that the market's prognosis is still positive for the fall.

The earnings yield backs up that forecast. The price/earnings ratio of the S&P 500 stands at 16, making the earnings yield 6.3% (1 divided by 16). The yield on the 10-year Treasury bond is only 3.6%. In March 2000, right before the market collapsed, the earnings yield was 3.9%, while the 10-year Treasury was paying 6.3%. "That would suggest that stocks are as cheap today as they were expensive back in 2000," says Freeman.

TO KEEP TRACK The Federal Reserve Bank of New York posts rate cuts in the Markets section at ny.frb.org. For the earnings yield, look up the S&P 500 P/E ratio in our Numbers section (page 130) and then divide 1 by that figure. Find the yield on the 10-year Treasury bond at our website, CNNMoney.com.

THE WILD CARDS A long, painful recession that hits corporate earnings hard or a spike in inflation that forces the Fed to start hiking interest rates again.

When Will My Home Be Worth More?

WATCH: INVENTORY
CURRENT READ:
NO RECOVERY SOON

→ **NATIONALLY**, high inventory levels are signaling a long slog for the housing market. But what you care about are prices in your town, where conditions may be dramatically different.

WHAT TO WATCH Locally, inventory is also the strongest price predictor, says Patrick Newport, a housing economist at Global Insight. Falling inventory—that is, fewer homes for

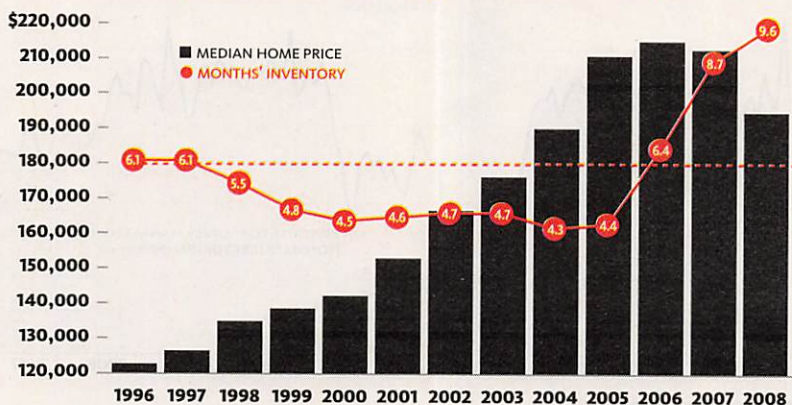
sale—bodes well for prices. Rising inventory is a sign of more price cuts to come. Inventory in Phoenix, for example, has been rising consistently for the past year, while median prices have steadily fallen.

FOR A SECOND OPINION While inventory represents the supply side of the market, the demand side of the housing equation is important too. For that, keep an eye on employment in your area. More jobs means more fresh buyers. Reading the business sec-

tion of your local paper is the best way to get a handle on job conditions in your city. Be on the lookout for big employers that are hiring—or downsizing.

TO KEEP TRACK The National Association of Realtors publishes national inventory only. Your local association of realtors tracks it in your specific market, where it matters most. So ask your broker. As an alternative, go online. HousingTracker.net posts the change in inventory for more than 50 big markets.

No Rebound Soon for Houses When the number of homes for sale falls below six months' worth, prices rise. Above six, they fall. Outlook now: still grim.



NOTE: Median price of single-family homes, inflation-adjusted. SOURCES: Bureau of Labor Statistics; National Association of Realtors.

When Will It Be Easy to Borrow Again?

WATCH: CREDIT SPREADS
CURRENT READ: CONTINUED TIGHT CREDIT

→ DESPITE AGGRESSIVE

Fed rate cuts, interest rates on 30-year fixed-rate mortgages have dropped, on average, by only about half a percentage point since last September. Rates on auto loans and credit cards have fallen even less. And more lenders are now reducing or completely freezing homeowners' ability to tap into their home equity, even for people with good credit.

You can blame this state of affairs on the ongoing credit crisis. Burned by the bad loans they made during the housing bubble, lenders are now looking at mortgages and other loans as far riskier than they did just recently. As a result, they're less inclined to lend in the first place. When will this freeze thaw?

WHAT TO WATCH Credit experts say to keep a close eye on the three-month "TED spread." This is the difference between the interest rate at which banks borrow from one another (known as Libor) and the rate on three-month Treasury bills. Since T-bills are essentially risk-free, the higher the TED spread, the more fearful banks are about lending. And if they're skittish about lending to one another, they're certainly not going to fall over themselves to lend money to you.

WHAT IT'S SAYING NOW More tight credit. The TED spread stands at 1.68%, far above historic levels. Kathy Bostjancic, a senior economist at Merrill Lynch, says the TED spread needs to come down to about 0.40% "before we can say the coast is clear."

TO KEEP TRACK You can calculate the TED spread at Bankrate.com. Search for the three-month Libor rate and the three-month T-bill rate. Subtract the T-bill rate from Libor and you've got it.



When Will My Job Feel Safe?

WATCH: STOCK PRICES
CURRENT READ: DEPENDS WHERE YOU WORK

→ **THE UNEMPLOYMENT RATE** stands at 5.1%, low by historical standards. But unemployment lags in recessions—it costs money to lay people off, so companies generally don't go down that road unless they are relatively sure a slowdown is here to stay. If we are indeed in a recession, history tells us that we can expect an additional 350,000 workers to lose their jobs every month until it's over. At some point the job losses will stabilize. How can you tell when your job is less at risk?

WHAT TO WATCH Take a cue from the stock market, advises John Challenger, CEO of outplacement firm Challenger Gray & Christman. The stock price is a forward-looking measure of a company's future earnings prospects. "You can't guarantee the market has it right, but it's a pretty good gauge to be looking at," he says.

Start with the performance of your industry against the market over the past few months. If it's been doing significantly better, that's a good sign that your field has already

started to rebound (or never faltered). Next, if your company is publicly traded, compare its stock price with the industry index. If the stock is up and if it has done better than the industry, the market is signaling that it believes management can grow in the coming months and years. That often translates into more hiring or at least no more layoffs.

FOR A SECOND OPINION It's also worth your while to keep your antenna up at work. You may know more than outside investors do. Are you being asked to scale back the budget? Are you hearing about products being discontinued? These could be warning signals.

WHAT THEY'RE SAYING NOW Of the 10 major sectors in the S&P 500, six have outperformed the broader index over the past year. So if you're not working in the financial services industry or for a business that is heavily reliant on discretionary spending, odds are decent that your job outlook may be fairly optimistic.

TO KEEP TRACK You can retrieve your firm's stock price at CNNMoney.com. Once you do, click on the Advanced Charts tab for industry and market matchups. \$

FEEDBACK: jrevell@money.com

JELD-WEN PRESENTS:

ONE-TO-ONE:

*A Design Guru Discusses Ways
to Give Your Home a New Look*

SPOTLIGHT ON: Kent Duckham, Architect

In his more than 20 years as an architect, Kent Duckham has found inspiration in a school of design established long before he was even born: the American Shingle Style. He has applied its familiar forms and details to his firm's residential renovation and expansion projects as well as to his designs for new homes. "I like the freedom it offers," he says.

The Boston-based architect steadfastly believes in the role of design in improving people's lives. "Good design can serve individual needs and add richness with superior materials and finishes," he says. "Windows are a big part of our design effort, and they have to reflect the quality of the rest of the project. The best have

details that are more refined, operate easily, and contribute to energy efficiency and a healthy home environment. That's what makes the JELD-WEN wood and clad-wood windows such a good choice because they satisfy all those criteria."

One of his projects involved adding a second floor to a basic '50s rancher in nearby Newton, Mass. "We basically doubled the size of the house, and since the original windows were obsolete, we put in all-new JELD-WEN windows built with AuraLast wood. That allowed us to take advantage of light and views. With their elegant style and excellent performance, the windows were definitely part of the project's success." ●

*Good design can
serve individual
needs and add
richness with
superior materials
and finishes.*

IMPROVEMENT STARTER QUESTIONS



1. What is the architectural style of your home? If you feel it lacks style, what type of architectural design would you like it to have?
2. Are there any design details, shapes, colors, or other elements you want new windows and doors to match or complement?
3. Do you want any windows with unique, custom shapes or sizes?
4. Have you developed a budget for your project?
5. Are you concerned about resale value or are you planning on living in the house for a long time?

JELD WEN
WINDOWS & DOORS

Here's your chance to win an Improvement Consultation from one of our experts.
Simply e-mail your first and last name, address, and phone number to

MONEYsweeps@winconsultation.net

See page 129 for complete Official Rules that govern this sweepstakes.



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Clad-Wood Double-Hung Window and 412 IWP® Custom Wood Exterior Door

With reliable JELD-WEN® windows and doors, any remodeling project becomes more enjoyable.

In fact, their lasting durability and long warranties ensure you'll have fewer worries—and greater peace of mind. We also offer a wide range of styles and options that let you beautifully restore or update your home's architecture. To learn more, call 1.800.877.9482, ext. 77225, or visit www.jeld-wen.com/77225.



RELIABILITY for real life®

JELD-WEN.
WINDOWS & DOORS



BIG- PICTURE GUY

PHOTOGRAPH BY HENRY LEUTWYLER

The godfather of global investors, **George Soros** retired as a multibillionaire. But now he's back, hedging his wealth against what he calls the worst economic crisis in 75 years.

BROKE AND FRIENDLESS IN POSTWAR LONDON, having just spent his last penny on food, 22-year-old George Soros made the first of a lifetime of prescient economic calls. "I have touched bottom," he told himself, "and I am bound to rise." As it turned out, the Hungarian-born survivor of both Soviet and Nazi occupations would do more than merely rise. He would parlay an uncanny flair for anticipating global economic trends into one of the great investing records of all time—not to mention a fortune estimated at \$9 billion. Soros retired in 2000 from running hedge funds and delegated control over a large part of his endowment fund to outside managers. But when subprime defaults began to ricochet around the world, he decided, at 77, to start investing again and to put his take on the crisis into a book, *The New Paradigm for Financial Markets*. He recently spoke to managing editor Eric Schurenberg.

Q. In your 50 years in finance you've seen any number of crises. Why is this so bad?

A. Because two bubbles are deflating at once. There's the collapse of housing prices, of course. On top of that there's the end of what I call the superbloom of credit expansion that has been going on for 25 years. That was made possible by a stable global financial system in which the dollar was the world's primary currency. Now, for many reasons, the system is in question and nothing has taken its

place. That has created great uncertainty.

Q. And for us regular people it means...?

A. The days of rapid financial wealth creation are over. We're now in a period of wealth destruction. It is going to be very hard to preserve your wealth in these circumstances.

Q. Don't feel you have to sugarcoat your answer just for my sake.

A. Since the 1980s, the global financial system has been dominated by an ideology I call market fundamentalism—the

idea that markets are perfect and regulations are always flawed. But markets aren't perfect. Left to their own devices, they always go to extremes of either euphoria or despair. The Federal Reserve and other regulators should recognize this, since they've had to bail out the markets in crisis after crisis since the 1980s.

Q. Can't the Fed just bail us out again?

A. The Fed's first duty is to prevent the financial system from collapsing. It's shown it can do that, and the markets are breathing a sigh of relief. But we can't avoid the fallout in the real economy. We're facing not only recession but also inflation and a flight from the dollar. To fight recession, the Fed needs to increase the money supply, but that only makes the dollar weaker and inflation worse. That's why I think this crisis is so serious. The Fed's power to intervene is limited.

Q. Where is your money now?

A. Mostly in my endowment fund, a good portion of which I had farmed out to other money managers. When I saw what I considered the most serious financial crisis of my lifetime, I came out of retirement and set up an account to hedge their positions.

Q. How?

A. I went short [bet against] the dollar, U.S. and European stocks and Treasury bonds. I went long [invested in] emerging markets. That worked last year, but this year bonds kept going up and emerging markets down. So I'm about even.

Q. Should MONEY readers do the same?

A. You'd have to be pretty nimble. I think most investors would be best off in safe, inflation-indexed Treasuries, even though they're quite expensive now.

Q. Growing up in Nazi-occupied Hungary must help you keep today's risky markets in perspective.

A. I'd agree that the prospect of extermination was a formative experience for me. [Laughs.] The Nazis taught me that the abnormal can become normal.

Q. And the lesson in that?

A. It's important in life and in investing always to question yourself. Understand that you may be wrong, especially when you believe too firmly that you're right.

Q. Have your billions made you happy?

A. I'm reasonably happy, but the money's not the point. It's an indication that I've succeeded in the grand adventure of understanding reality. **\$**







THE HIGH COST OF A GREEN DREAM

It seemed like a fantasy project to renovate their new home in an environmentally sensitive way. Reality is costing them more green than they could have imagined.

By Paul Keegan

Photographs by
Andrew Hetherington

AS A GIRL IN SOUTH KOREA, HyoJung Kim did her schoolwork on brownish-gray recycled paper and rarely threw things away because government-mandated garbage bags cost \$1 apiece. Arriving in the United States for graduate school, she was stunned to see trash piled high on city sidewalks and documents printed on a single side of white paper. In her home country, with 48 million people jammed into an area the size of Ohio, HyoJung says, "Our attitude is, 'How *dare* you waste that?'"

With such an upbringing, it's no surprise that HyoJung, now an urban designer in Washington, D.C., was

"green" long before that term connoted "cool." She married fellow architect and conservation enthusiast Seth Garland last fall, and they bought a four-bedroom Capitol Hill townhouse that they decided to gut and make as green as green could get: from energy-saving light fixtures and appliances down to the framing, plumbing and insulation.

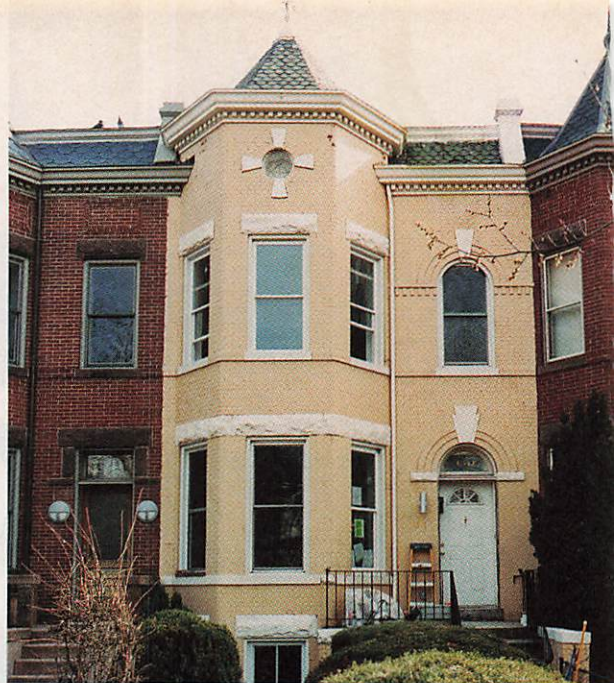
But going green, the couple are now discovering, can quickly land you in the red. Seth, 37, and HyoJung, 34, thought the job would take three months and cost \$70,000, with them shouldering some of the work. Six months in, they now estimate it will cost twice that much in money and elbow grease. Seth says he was "shocked" by the cost of some green upgrades. "I found a more efficient tankless hot-water system for \$1,500, but the contractor told me it would cost \$6,000 to install it." They're working late into the night laying bathroom tile themselves to save money.

Meanwhile, they have drained most of their savings and can't afford to keep living in HyoJung's condo in Gallery Place and paying the mortgage on the new house too. They've even got a third place: a house Seth bought in nearby Silver

Spring, Md. years ago that is now rented out. All told, the couple hold three adjustable-rate mortgages that add up to more than \$1 million on a combined salary of just under \$120,000—and in a real estate market that's only headed lower. Plus, they're underfunded for retirement, with a mere \$75,000 in tax-deferred accounts. "Their situation is very worrisome, absolutely," says Chuck Bender of the Financial Consulate in Lutherville, Md., who reviewed the couple's finances at MONEY's request. "They have very little margin for error."

THE PERFECT PLACE

HyoJung and Seth met three years ago at her architectural firm in Silver Spring, where he was a summer intern. He looked so young she was surprised to discover that he is almost four years her senior and already had a career as a litigator before studying architecture. Both were recovering from divorces and in no hurry to get involved again, but eventually Seth moved



into her condo. Last spring, as they took an early Sunday morning walk near the Washington Monument, Seth dropped to one knee and pulled out a ring. It wasn't a complete surprise—knowing her strong tastes in design, he had already asked her to choose from several styles—but still, HyoJung burst into tears.

Hoping to start a family, they began looking for a larger home. In September, a few weeks before their wedding, they found a 1912 brick house with lovely bay windows and a basement they could convert into a rental apartment. At \$550,000, it was about \$75,000 more than they had planned to spend, but it had the advantage of being near several subway lines. They could get rid of their car. Seth, a big booster of mass transit, has helped design subway stations and light rail systems in Maryland and northern Virginia.

Taking on so much real estate debt came with risk, but Seth has had success renting out his house and HyoJung's family did well as property investors in Korea. And the new place offered a dream project. "From the very beginning," says HyoJung, "we said, 'Let's make it green.'"

GREEN TAKES A LOT OF GREEN

The couple decided to turn one of the four upstairs bedrooms into a master bathroom. On the first floor they knocked down the walls to turn the living room, dining room and kitchen into one large, open space—both for aesthetic reasons

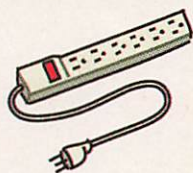
GET MORE GREEN FOR YOUR GREENBACK

While installing a green heating/cooling system or plumbing infrastructure in your home can be expensive, there are plenty of environmentally friendly steps you can take that won't cost much.



▲ **LIGHT A CANDLE,** blow it out and place it by the window. "If you see the smoke blowing around, there's a leak that can be sealed up," says Bambi Tran, a consultant with Sustainable Design Consulting of Silver Spring, Md. "Remember, caulk or foam sealant is cheap."

✦ Cooking with a microwave oven expends much less energy than using a stove or even a toaster oven.



▲ **CONNECT ELECTRONIC DEVICES** to surge protectors so you can cut off power when not in use.

✦ Place your lamps in corners to better reflect light off walls instead of lighting the entire room. Connect lights outside the home to motion sensors.

✦ Clean the condenser coils of your refrigerator every six months to improve airflow. Fix or replace broken seals on the door.



▲ **USE A CLOTHESLINE.**

Hang one in your laundry room. It keeps the dryer off and adds moisture to the air during winter.

✦ Turn your hot-water-heater settings down to 120°F from the standard 140°F—the water should still be hot enough for showers. Put an insulating jacket around the hot-water heater.



CONSTRUCTION ZONE

At right, HyoJung works in the living room. Attic insulation will cut energy costs. Above, the couple check out samples of cork and bamboo, greener alternatives to plywood, to use as subfloor. At left, the view from the street of their new home.

and to allow cross-ventilation that will cut air-conditioning costs.

Some choices were obvious: They used studs from suppliers that employ sustainable timber-harvesting practices; applied spray-foam insulation on the underside of the roof to keep the attic cool in summer; installed energy-efficient compact fluorescent lighting; and sprang for argon-gas double-paned windows (at \$400 each) for better insulation. For subflooring they opted for oriented strand board, made of wood scraps, instead of plywood. They sold their old doors, metal pipes and radiators to salvage yards and installed water-efficient toilets and faucets.

But they were dismayed to find out how much they couldn't afford. Seth had planned to install energy-efficient polyethylene tubing called PEX, but the plumbers who could work with the material would be too expensive. The couple had to settle for nonbiodegradable plastic pipes instead. They also had to give up radiant floor heating—tubes of hot water under the floor that can lower energy costs—because the insulation required would be too expensive. Also scratched were a roof that would support a garden and keep the house cooler in summer, a \$12,000 solar hot-water system and a solar electric system that would set them back at least \$20,000 (costs only minimally offset by federal tax credits of \$2,000 for each solar-powered system).



SIX MONTHS INTO THE PROJECT, THEY ESTIMATE IT WILL COST TWICE WHAT THEY HAD BUDGETED.

By April, Seth's \$70,000 in savings from his days as a lawyer had evaporated, and the \$25,000 it would cost to get the house into bare-bones living condition would just about wipe out the cash HyoJung had put away. Meanwhile, each month they couldn't move in and get a renter into her condo cost them another \$2,000. The answer? Another loan. HyoJung took out a home-equity credit line on her condo.

With remodeling costs out of control, cherished green projects on hold plus an awful lot of mortgage debt, Seth and HyoJung sat down with a financial planner, an alternative-energy expert and a green remodeling consultant for advice about how they could become more green and more financially stable.



SELL HYOJUNG'S CONDO

Being so highly leveraged has not only disrupted Seth and HyoJung's green-ing plans, it has also put them at serious financial risk, says Bender of the Financial Consulate. If one of their rental properties goes empty or unforeseen repairs crop up, they could easily slide into negative monthly cash flow.

The solution: sell HyoJung's condo—fast. A year ago it would probably have sold for \$430,000, but its market value has dropped to \$415,000 and is likely to continue falling, according to Tom Murphy of Long & Foster realtors. Selling Seth's house in Silver Spring makes less sense because it's rented and the couple may eventually move back to that family-

oriented neighborhood and its good schools.

The condo sale should generate about \$140,000 after HyoJung pays off her mortgage and credit line, and the proceeds could be used for several important purposes: They would allow the couple to diversify their holdings so they're not as dependent on real estate. They can each fully fund Roth IRAs for this year (\$10,000 total) and increase their combined 401(k) contributions for 2008 from \$4,800 to \$30,000. (With the condo expenses gone, that should be their goal in the future too.) Since they're young, Bender says, the couple can afford to be aggressive in their retirement accounts, with an all-stock-fund portfolio that includes international equities and natural resources.

At the same time, though, Bender wants them better protected in the short term. He suggests they pay off their \$10,000 in credit-card debt, put \$30,000 into an emergency fund and set aside another \$20,000 that could be used to offset some of HyoJung's lost income if, as planned, she has a child and decides to stay home for a while.

Finally, they can put \$25,000 toward completing the work that would make the house livable, which includes finishing the basement and master bathroom, as well as installing kitchen flooring and cabinets. That still leaves \$20,000 for green renovations they had given up on.

GET GREENER

It's too late to do anything about the plastic plumbing and lack of radiant floor heating, but \$20,000 would pay for several green improvements. Paul Wittemann, a solar power entrepreneur and certified energy auditor with Greenspring Energy of Towson, Md., suggests they start with a venting skylight (\$2,000) over the second-floor landing, frequently a dark spot in older homes. That will create airflow to cool the house and will allow natural light into the second floor and staircase, reducing the need for electric lights during daytime.

Another \$6,000 should go for a new

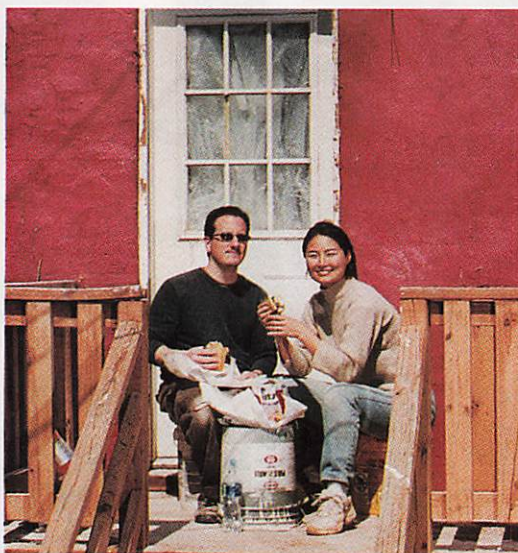
boiler with an Energy Star rating. Seth and HyoJung had decided to save money by not replacing the existing boiler. But according to Bambi Tran, a green consultant with Sustainable Design Consulting of Silver Spring, that old boiler will end up costing them more in the long run. "The better Energy Star boilers could save them thousands of dollars in fuel consumption," she says, "and would be much better for the environment."

They would still have enough left over for a solar hot-water system. "That can produce 70% to 80% of their house's hot water, saving substantially on energy bills," says Wittemann.

Seth and HyoJung initially resisted the idea of a bunch of experts coming into their home and giving them advice about their area of expertise. But now they're glad they did. "And we thought we knew everything," says HyoJung.

The couple were also initially against selling the condo, hoping to weather the current downturn. Renting the place out proved harder than they thought, however, and HyoJung started getting nervous about covering all those mortgage payments. When an offer to buy the condo for \$410,000 fell into their laps, they decided to take it. Bender was right, they realized, and it was a relief to know they could pay off their debts and fully fund their retirement accounts.

As for those green improvements they can now afford, "We're not running out today to buy all that stuff," says Seth. As



THE BOTTOM LINE

Seth Garland and HyoJung Kim need to cut their exposure to real estate and free up cash to finish their green dream.

+ INCOME

Salaries	\$117,250
Rental income	22,800
Withdrawals from savings	94,000
HELOC proceeds	6,000
TOTAL	\$240,050

- OUTGO

Renovations on new home	\$100,000
Mortgages, property taxes, insurance	75,580
Income taxes	13,980
Dining out, entertainment, travel	12,050
Groceries	5,900
Savings	5,000
401(k) contributions	4,830
Legal expenses (HyoJung's green card)	4,000
Home maintenance, utilities	3,630
Cell phone, cable, Internet	2,880
Parking	2,820
Public transportation	2,400
Car insurance, gas, maintenance	2,000
Clothing	1,500
Gifts	1,200
Pet expenses	600
Subscriptions, books	600
Charitable donations	600
Professional associations	480
TOTAL	\$240,050

+ ASSETS

Capitol Hill house	\$650,000
Silver Spring house	425,000
Gallery Place condo	400,000
Retirement accounts (401(k)s, IRAs)	75,335
Stocks and mutual funds	53,279
Checking and savings accounts	32,204
TOTAL	\$1,635,818

- LIABILITIES

Capitol Hill house	\$521,833
Silver Spring house	253,848
Gallery Place condo	235,832
Credit cards	10,000
Home-equity line of credit	6,000
TOTAL	\$1,027,513

= NET WORTH

\$608,305

of mid-April, the couple are still putting in long hours to make the house livable within a few weeks, when they expect the condo sale to close. "After we move in, we're going to take a little rest and regroup," Seth says with a chuckle. "Frankly, we're a little tired." \$



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APPLIANCES

The Power of Induction

The ultimate kitchen upgrade: a cooktop that cooks twice as fast—but won't burn the kids' fingers

BY SALLY SCHULTHEISS
PHOTOGRAPH BY JOHN KUCZALA

> MAGNETIC INDUCTION MAY JUST BE the best technology to hit the kitchen since the microwave oven. In the past few years this style of cooktop, which turns magnetic energy into heat, has proved itself a worthy competitor to the traditional choices—gas and electric. And while induction has only recently

joined the list of options, some experts already predict it will soon become an essential value-adding addition for kitchen remodels. After all, it's faster, safer and more efficient than anything before, says Francisco Migoya, an assistant professor at the Culinary Institute of America in Hyde Park, N.Y. He cooks with it; maybe you should too.

WHAT INDUCTION IS

An induction cooktop looks a lot like an electric smoothtop, but what goes on beneath the surface is very different. Instead of an electric element, an induction stove is centered around a powerful magnetic copper coil, which creates a high-frequency electromagnetic field when electricity is turned on. Put a pot made of a magnetic material—like iron or steel—onto that field and the energy gets transferred to it in the form of heat. Nothing else gets hot, only the pot, and you can adjust the field and the heat with the knob, just as with your old stove.

WHERE IT CAME FROM

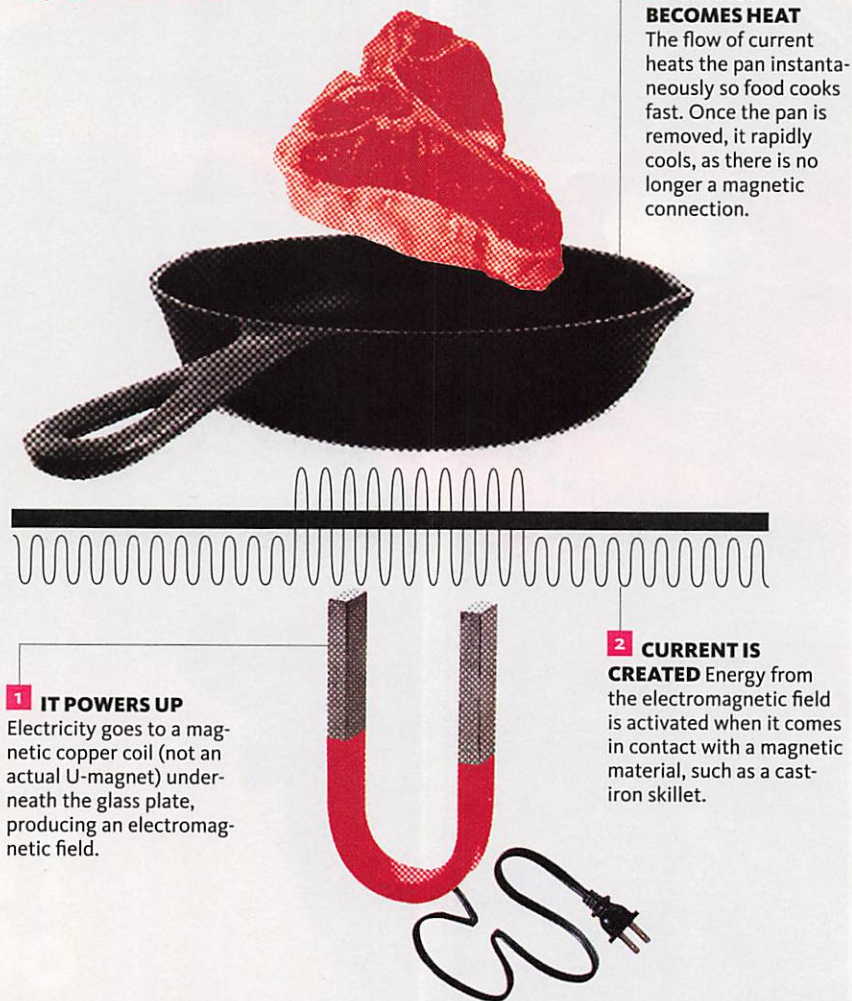
Even the greatest technologies take a while to catch on—though induction has probably taken longer than most. The science behind it was actually discovered back in 1831 by physicist Michael Faraday. It would be more than a century, however, before companies started using induction for anything other than industrial applications. (The same technology is used in generators and transformers.)

By the 1970s, manufacturers in Europe and Asia finally began experimenting with cooking uses, and the technology took off quickly on those continents. But American firms weren't as successful at marketing what was then an almost prohibitively expensive product. By 2000 all the induction stoves of that generation had been pulled off the U.S. market, says Eric Walker, a former electrical engineer who now sells cooktops via theinductionsites.com.

In the past two years, induction manufacturers have returned full-press with a different approach. "They seem to realize that the way to present the product is to the upper-market segment, rather than to storm the walls of the slide-in 30-inch

HOW IT WORKS

These cooktops harness the power of magnetic energy to cook your dinner. Here's what happens when you turn the knob.



ranges," says Walker. At the Kitchen and Bath Show in Chicago this April, several new induction cooktops were introduced, joining the 65 or so already on the market from prestigious players like Bosch, Electrolux, Thermador and Wolf. Everyday brands GE and Kenmore are making them under their high-end lines; even gas king Viking is in the act. "This is definitely an expanding product category," says Rick Demert, a buyer for Sears. Last year the retailer carried three induction models; Demert expects it will have 20 by year-end.

This time, induction is here to stay.

WHAT'S SO HOT ABOUT IT

Induction offers several advantages over gas and electric:

> It's more powerful. Some 86% of the heat in induction cooking goes to the pan—as opposed to 40% with gas and 52% with electric. Walker says a 2.4-kilowatt induction cooktop—a middle-of-the-road model—provides roughly the same oomph as an ultra-high-end gas cooktop with 17,000 BTUs. Also, since induction cooktops emit less extraneous heat, no hood ventilation is required. (Still, don't expect major electric savings. Walker estimates \$35 a year.)

➤ **It's faster and more precise.** Because the unit heats up instantaneously and uses more of the energy, you can boil a quart of water on an induction cooktop in just over two minutes. Also, "The temperature precision makes it better for delicate tasks like caramelizing sugar and melting chocolate," says Chef Migoya of the Culinary Institute. (As manager of one of the school's restaurants, Migoya outfitted his professional kitchen with induction.)

➤ **It's safer.** Since the heat goes straight into the pot without escaping to the cooking surface, you can touch the element even when it's on, a nice safeguard for those with small children at home.

➤ **It's easier to clean.** A common frustration with electric smoothtops is that bits of food become stubborn blemishes once they cook on. Because the induction unit stays cool, drips wipe right up.

WHAT'S NOT SO HOT

➤ **You need certain pots and pans.** Only cookware that's ferrous—a fancy word for magnetic—conducts the energy. That means iron, steel and some types of stainless steel (a high nickel content will render it nonmagnetic); some All-Clad and Calphalon pieces are compatible. The best test: If a magnet sticks to your pan, it's good. But if you're a ceramic cookware buff or you're wedded to your clear Pyrex saucepan, induction cooking is not for you.

➤ **You'll pay top dollar.** Prices for built-in induction cooktops now go from \$1,500 to \$3,500, significantly higher than basic gas or electric stoves. "And this isn't like the plasma TV, where prices will plummet in the next few years," says Sears' Demert. Still, as he notes, the prices are comparable to those of top-of-the-line gas cooktops, which can go as high as \$4,200.

➤ **You can't get the whole package.** Right now induction is available mainly in cooktops, and that can make installation difficult. Only one full range (meaning oven included) has come out so far (price: \$9,500). "So you see, there's a vast market waiting to be tapped," Demert says.

➤ **It's an adjustment from gas.** Many gas users prefer the "style" of gas cooking, finding it easier to adjust the heat by looking at the flame level, says Mars Iletto, a sales associate at Bay Cities

Kitchens & Appliances in Santa Monica, Calif. The efficiency of induction can also throw off a gas cook's pacing; there's barely time to grate the Parmesan before the pasta water is ready. Iletto notes, however, that rarely does an electric-cooktop owner enter his store who cannot be persuaded to convert to induction.

HOW TO SHOP

Think you're ready to be converted? First step, check out what's out there. Start at appliance retailers like Home Depot, Lowe's and Sears, which have growing selections of low-end and moderately priced units; for higher-end models, you may need to visit kitchen design centers.

Then determine what you'll want. The first choice is built-in or freestanding. If you already have a separate cooktop, you may be able to easily replace it with a built-in model; standard sizes for induction are 30-inch with four elements and 36-inch with five. If you now have a full "slide-in" range, on the other hand, you'll need to invest in an undercabinet oven,

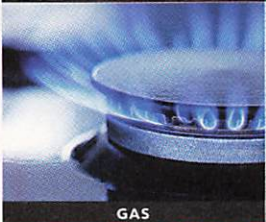
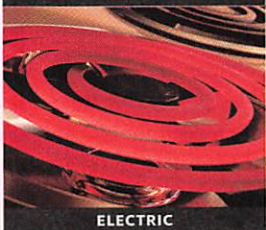
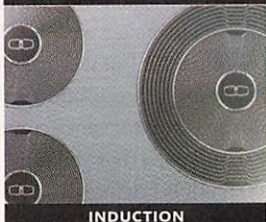
and you'll need to whack out part of your countertop to make room for the cooktop. In that case, unless you're planning a full kitchen reno, it might make more sense to get a freestanding plug-in unit, which generally has one element and starts at \$80.

Next, as with any stove installation, you must figure out what kind of wattage your wiring can support. (Though induction is more efficient, it uses the same energy input as a normal stove to achieve higher cooking power output.) To calculate your potential cooking power, multiply the amperage of your circuit breaker (listed on the box) by 0.24, says Walker. If you have 50 amps, you can look at models up to 12 kw. Be aware that some units "power share," which means all elements cannot achieve highest power at once.

Finally, if you want to embrace the new technology but aren't ready to buy in all the way, consider a hybrid model—a cooktop that offers a combination of radiant electric elements and induction elements. These start at about \$1,500 and will give you a taste of what's to come. \$

HOW INDUCTION COMPARES

The latest stovetops offer lots of benefits, but you'll pay big money for them.

STOVE TYPE	INDUCTION IS FASTER...	...AND MORE EFFICIENT	...BUT MORE EXPENSIVE
 GAS	How long it takes to boil one quart of water: 5 MINUTES	How much power goes into the pan: 40%	How much you'll pay: \$1,300
 ELECTRIC	9 MINUTES	52%	\$250
 INDUCTION	2½ MINUTES	86%	\$2,500



Best-Picture Nominees

A new wave of camcorders can maximize video for HDTV for less than \$1,000 **BY CHARLES PASSY**

You got a high-definition television so you could appreciate every detail of your favorite shows. So why not devote that same attention to the movies you make yourself? An HD camcorder can turn your vacation into a summer blockbuster.

Until recently, buying one of these cameras could have set you back as much as \$1,500. But in the past year, several manufacturers introduced entry-level models under \$1,000. And with high-def TVs in 41% of American homes, according to the Consumer Electronics Association, the appeal is as clear as the picture. If you're a home-movie maker with HDTV in the living room, the question should not be *if* you'll get an HD camcorder but *which* to get.

The top consideration is picture quality. By definition, HD means higher resolution: up to 1,080 lines vs. 480 lines with standard definition. But the key phrase is "up to," since some models have only 720. As shown by our test, higher is crisper—so much so that you may not want to bother with a 720, even if your TV is 720p. The 1,080 models are more expensive, but you can get in under \$1,000 if you skip the bells and whistles. (One nice perk:

SONY'S HDR-UX10

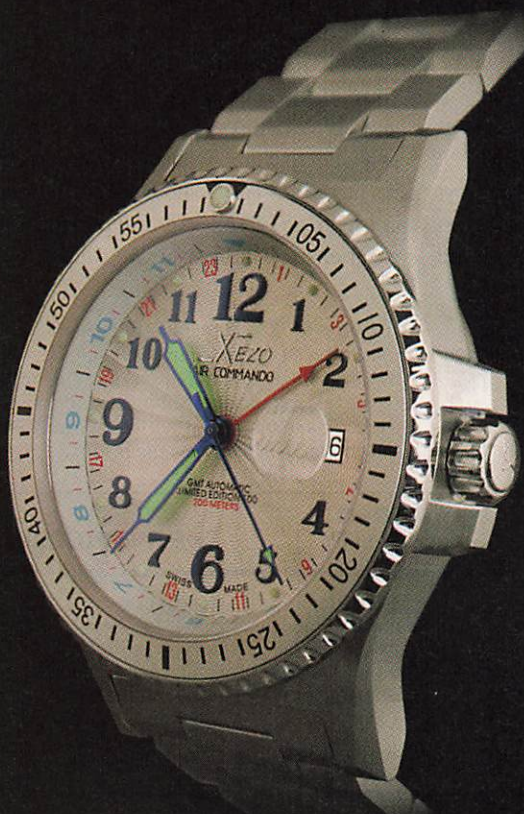
This high-definition camcorder was a clear winner because:

- > It delivered a crisp picture with realistic color.
- > It's relatively simple to operate.
- > It comes with such helpful features as Face Detection (allows for better focusing) and Quick On (makes it easier to start camcorder from sleep mode).

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Xezo is now offering the Air Commando limited-edition watch at the below-retail introductory price of \$584.00 USD for a limited time. Free shipping to U.S. customers. To order, visit the manufacturer's Web site at www.Xezo.com or call (800) 779-0102 within the U.S.

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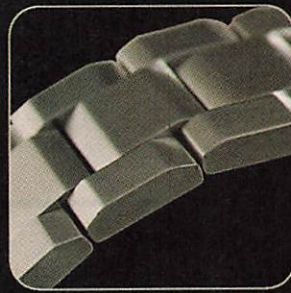
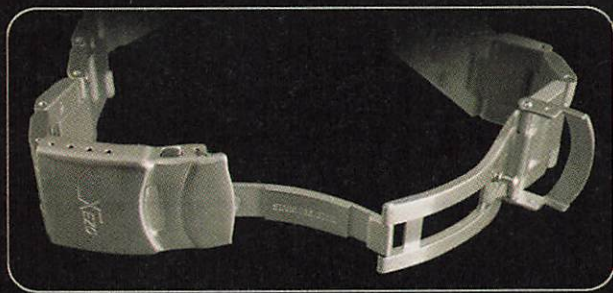
SAPPHIRE CRYSTAL GLASS FRONT & BACK

SILVER FACE:
LUMINOUS HANDS & MARKERS

BLACK FACE:
LUMINOUS HANDS, NUMERALS & MARKERS



The Swiss-made, automatic Air Commando by Xezo is built to last



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Even low-end cameras take still pictures.)

The other big and dizzying decision is format. HD camcorders come in a variety of recording media—some even offer more than one. The basic choices:

➤ **TAPE (A.K.A. HDV)** A pop-out format with an hour or so of recording per tape, HDV is a good option if you like to physically archive videos. But it can be pricier than other formats, and tapes run up to \$10 each. As with VHS, you'll need to do a lot of fast-forwarding and rewinding.

➤ **MINI DVD** Same convenience and ease of archiving, and you can speed ahead to certain tracks. Cons: DVDs can scratch, and they store as little as 15 minutes.

➤ **FLASH MEMORY** These use cards, as

in digital cameras, and sometimes internal memory too. Some cards record two hours; at \$80-plus apiece, though, these add up.

➤ **HDD (BUILT-IN HARD-DISK DRIVE)** There's no tape, card or DVD to buy, and you get up to seven hours of recording. But you'll eventually have to dump videos to a computer—a pain while traveling.

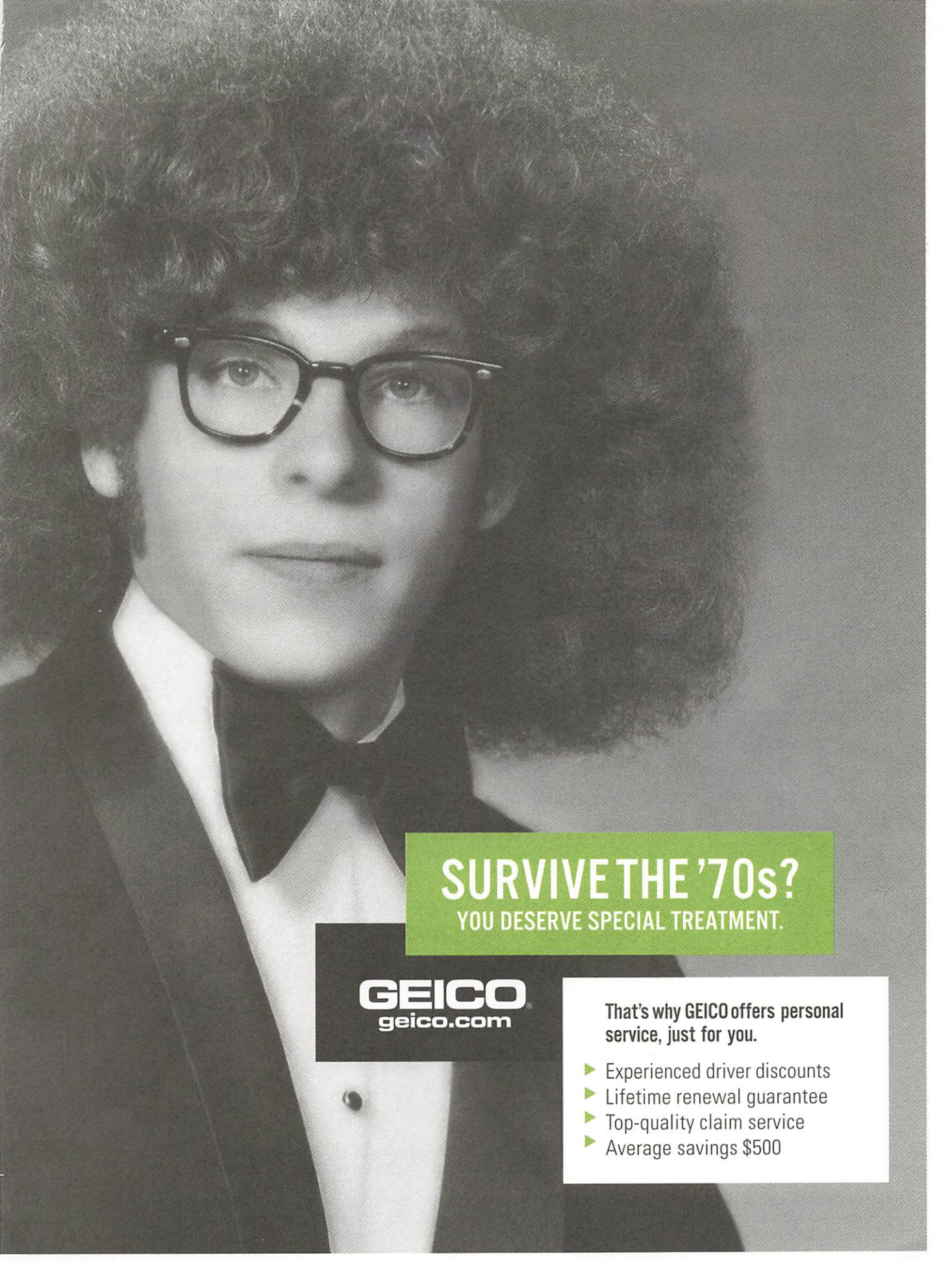
Of all the formats, "flash is the future," says David Kender, editor of Camcorderinfo.com. But until prices come down on cards, mini DVD is probably the best value for the least hassle, as our test found. Of course, every format has its fans. Kender believes even tapes, the oldest technology, will be in stores for at least five more years.

It's worth noting that while all these

camcorders make it possible to transfer HD video to a computer and edit it, so far playback is a challenge. If you burn the movie to a regular DVD, you must downgrade it to standard resolution; to maintain quality, you'd need a Blu-ray burner (\$350-plus) and player (\$450 and up). That said, if you just want to watch what you've recorded, it's incredibly easy to hook up an HD camcorder to an HD television and relive your vacation in all its breathtaking detail. **\$**

How we did it We picked the highest-resolution HD camcorder under \$1,000 from five prominent manufacturers, put the models to the test indoors and outdoors, and enlisted cameraman Bob Leak of WPTV in West Palm Beach, Fla. to help review the results.

		EASE OF USE	VIDEO QUALITY	THE BIG PICTURE
SONY HANDYCAM HDR-UX10 \$600 and up				
FORMAT DVD and flash stick RESOLUTION 1,080 lines ZOOM 15x		SCREEN 2.7-inch-wide LCD (also has eyepiece viewfinder) WEIGHT 1.2 pounds with battery	Intuitive and comfortable. ("Well balanced," said pro cameraman Bob Leak.) Extras like Face Detection, for focusing, are handy. HARD ————— EASY	Remarkably sharp for a low-priced high-def model. Leak was particularly impressed with how it performed in dimmer lighting. ★ ★ ★ ★ ★
JVC EVERIO GZ-HD3 \$685 and up				
FORMAT Hard disk, flash card RESOLUTION 1,080 lines ZOOM 10x		SCREEN 2.8-inch-wide LCD (no eyepiece) WEIGHT 1.5 pounds with battery and strap	User-friendly controls and a screen with a sharp display are big pluses. On the downside, it's the heaviest of our tested units. HARD ————— EASY	"Pretty crisp," Leak declared. He thought flesh tones came out better than on most other units. ★ ★ ★ ★ ★
CANON VIXIA HV30 \$850 and up				
FORMAT HDV (tape) RESOLUTION 1,080 lines ZOOM 10x		SCREEN 2.7-inch-wide LCD (has eyepiece) WEIGHT 1.3 pounds with battery	Bulky to hold but has easy button access. Tape was frustrating: lots of rewind and fast-forward required for viewing. HARD ————— EASY	Images were clear, but Leak complained that colors didn't "pop" enough. ★ ★ ★ ★ ★
SANYO XACTI VPC-HD1000 \$675 and up				
FORMAT Flash card RESOLUTION 1,080 lines ZOOM 10x		SCREEN 2.7-inch-wide LCD (no eyepiece) WEIGHT 0.7 pounds with battery	Slim, pistol-like design is very purse-friendly. But it's hard to keep a steady grip and operate controls if you have big hands. HARD ————— EASY	Good, not great, said Leak. He praised the colors ("nice, clean") but thought the images were blottier in indoor lighting. ★ ★ ★ ★ ★
SAMSUNG SC-HMX10 \$450 and up				
FORMAT Flash card and internal RESOLUTION 720 lines ZOOM 10x		SCREEN 2.7-inch-wide LCD (no eyepiece) WEIGHT 0.7 pounds without battery	Easy to operate, with touchscreen interface. But the unit kept forcing us to reformat, so we lost video. Samsung says it was an anomaly. HARD ————— EASY	Samsung's only HD offering is just 720 lines—and can't compete with our top performers. Leak complained of "lots of grain." Images were not as sharp. ★ ★ ★ ★ ★



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'my mom said, spinning around. r had been a PC guy since the days ers that existed. He learned how to of a wall. His favorite pastime was utting the hard drives in new ones. thirty half-dismantled computers

the switch," he said. "I want to get graphics programs work so much ox and ran his finger over the pic-

When I told you I was using one in i didn't speak to me for a week." uated and stubborn, which I have e. Macs are the way of the future." a million "Switch" commercials. re ship.

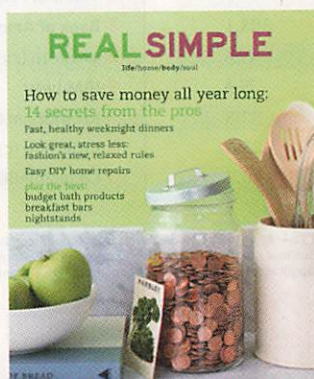
unusual he was acting? A PC-to-Mac ility than lipstick on the collar.

"he pronounced, running up to his woman is? This is the Ringling wife on earth!"

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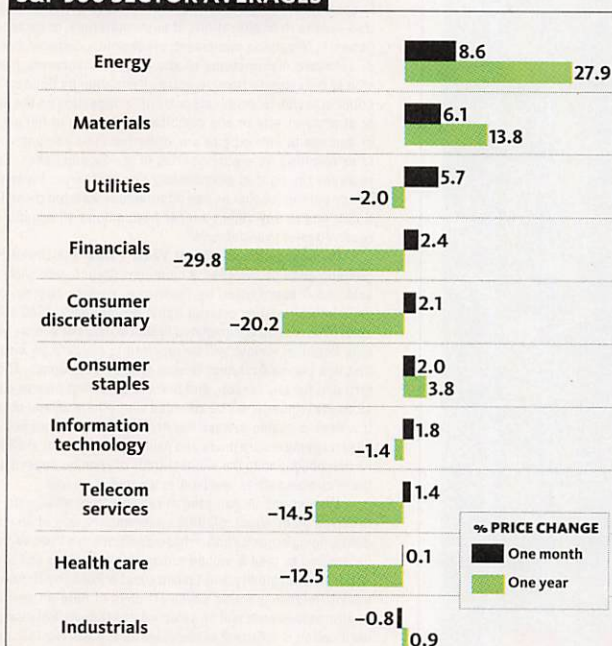
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Stocks

Equities Shine Brightly Thanks to Energy

The markets snapped back in the month ended April 17 as all the major stock indexes posted strong gains, led by the **Morgan Stanley EAFE index** of foreign stocks, which rose 8.8%. In the U.S. market, the **energy** sector soared thanks to a surge in crude-oil prices—which hit nearly \$115 a barrel during the month—boosting the shares of major oil companies like **ExxonMobil**, **Chevron** and **ConocoPhillips**.

S&P 500 SECTOR AVERAGES



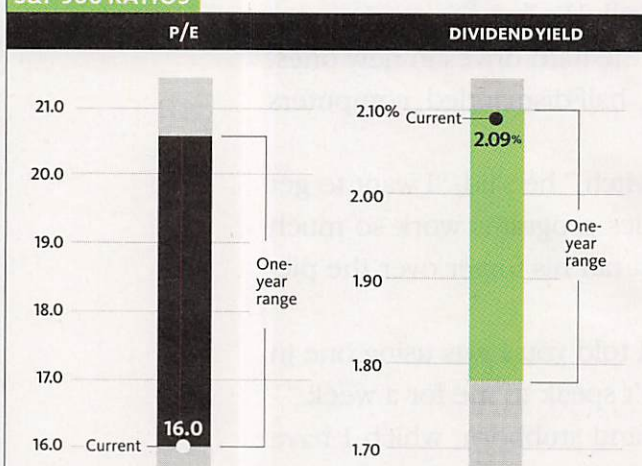
TOP-PERFORMING STOCKS

RANK	STOCK (TICKER)	PRICE	TOTAL RETURN	
			ONE MONTH	ONE YEAR
1	IPCS (IPCS)	\$30.51	77.7%	N.A.
2	Millennium Pharmaceuticals (MLNM)	24.50	71.9	105.9%
3	Bear Stearns (BSC)	10.15	71.7	-92.9
4	Vertex Pharmaceuticals (VRTX)	25.47	69.6	-19.5
5	Lindsay Manufacturing (LNN)	121.77	59.7	305.1
6	AbitibiBowater (ABH)	10.62	50.4	N.A.
7	Patriot Coal (PCX)	64.16	49.6	N.A.
8	McMoRan Exploration (MMR)	25.86	49.3	87.8
9	Corinthian Colleges (COCO)	10.39	48.2	-25.6
10	Massey Energy (MEE)	51.92	47.6	110.7

BENCHMARKS

INDEX	LEVEL	TOTAL RETURN		
		ONE MONTH	ONE YEAR	THREE YEARS ¹
S&P 500	1365.6	2.8%	-5.3%	7.5%
Nasdaq ²	2341.8	3.7	-6.5	6.3
Russell 2000	708.0	4.0	-12.5	7.4
Morgan Stanley EAFE	2106.8	8.8	-3.1	14.8
Dow Jones industrial average	12,620.5	2.2	0.9	9.6
Lehman Brothers aggregate bond	1299.0	-1.1	6.4	4.8

S&P 500 RATIOS



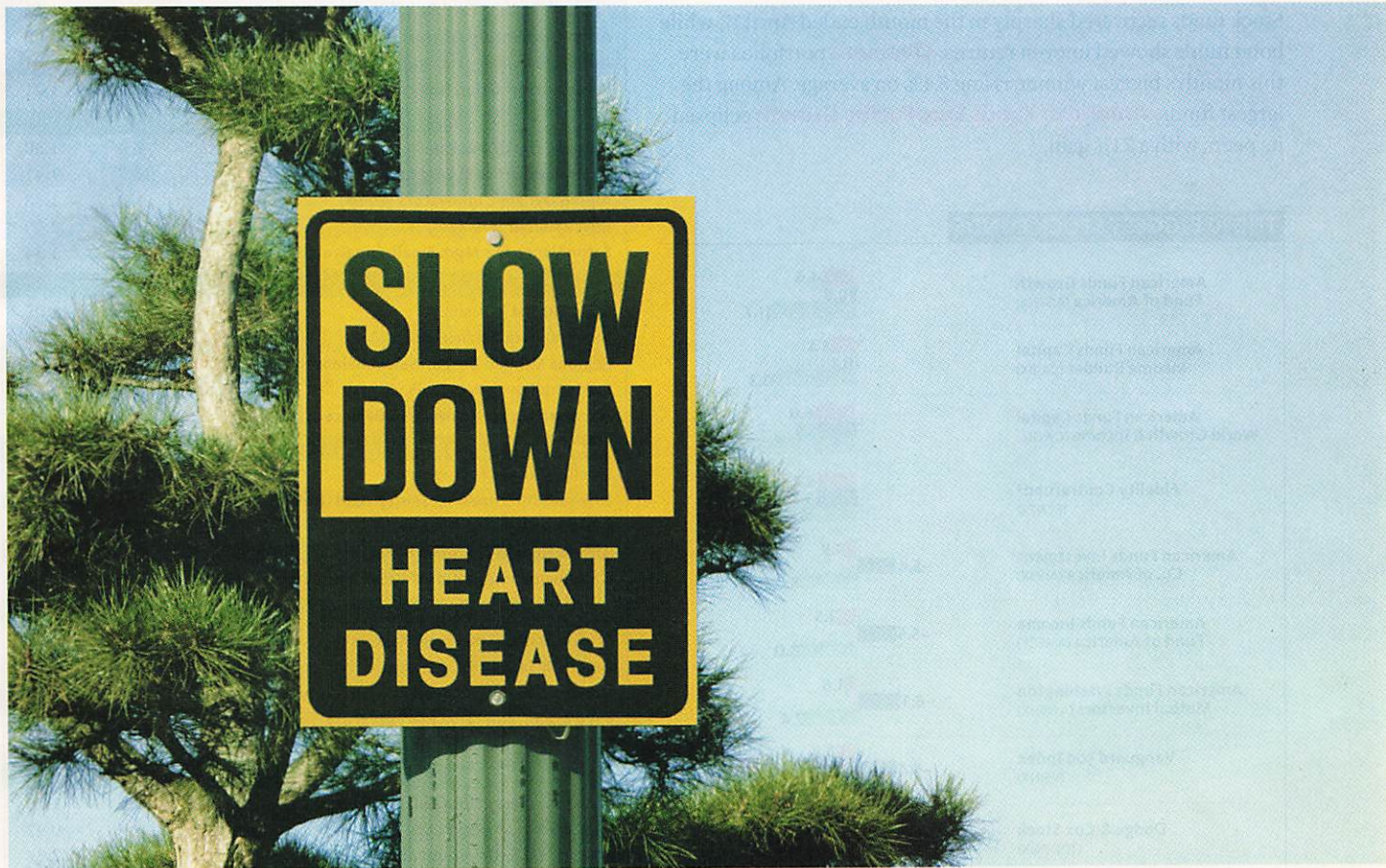
HIGHEST-YIELDING DOW STOCKS

STOCK (TICKER)	PRICE	DIVIDEND YIELD
Bank of America (BAC)	\$37.47	6.8%
Pfizer (PFE)	20.40	6.3
Citigroup (C)	24.03	5.3
General Motors (GM)	19.79	5.1
Verizon (VZ)	35.85	4.8
AT&T (T)	37.57	4.3
Merck (MRK)	39.22	3.9
General Electric (GE)	32.02	3.9
J.P. Morgan Chase (JPM)	45.12	3.4
DuPont (DD)	51.21	3.2

MOST WIDELY HELD STOCKS

RANK	STOCK (TICKER)	PRICE	TOTAL RETURN	
			ONE MONTH	ONE YEAR
1	ExxonMobil (XOM)	\$93.38	5.5%	21.2%
2	General Electric (GE)	32.02	-11.4	-5.5
3	AT&T (T)	37.57	2.4	0.3
4	Wal-Mart Stores (WMT)	56.67	11.2	20.0
5	Bank of America (BAC)	37.47	-3.8	-22.9
6	Chevron (CVX)	91.99	6.8	21.3
7	IBM (IBM)	123.08	3.9	31.5
8	J.P. Morgan Chase (JPM)	45.12	6.5	-10.4
9	Citigroup (C)	24.03	16.0	-51.0
10	ConocoPhillips (COP)	82.81	5.8	21.0

NOTES AND SOURCES: Unless otherwise noted, data as of April 17 from Lipper, New York; 877-955-4733. Index levels from Bloomberg. Bond index data from Lehman Brothers. Stock data from Thomson/Baseline. Monthly S&P 500 ratios from Standard & Poor's. Ratios are based on previous four quarters of operating earnings. Top-Performing Stocks limited to companies with market capitalization of at least \$500 million. Most Widely Held Stocks ranked by Standard & Poor's. N.A.: Not applicable or not available. ¹Annualized. ²Price change only.



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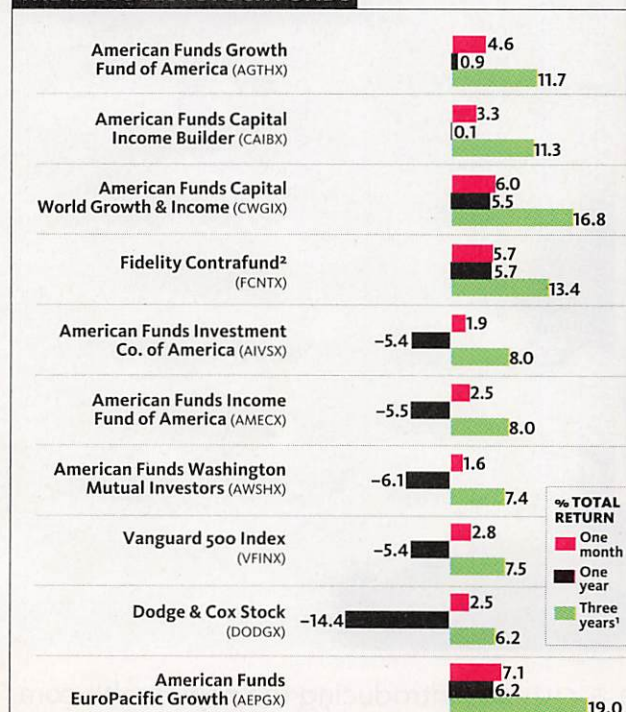
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Where to turn

Mutual Funds

Foreign Funds Soar as Market Rebounds

Stock funds recovered sharply in the month ended April 17, while bond funds showed uneven returns. **Overseas** portfolios were this month's biggest winner, rising 8.4% on average. Among the largest funds, **American Funds EuroPacific Growth** eclipsed its peers with a 7.1% gain.

THE 10 BIGGEST STOCK FUNDS



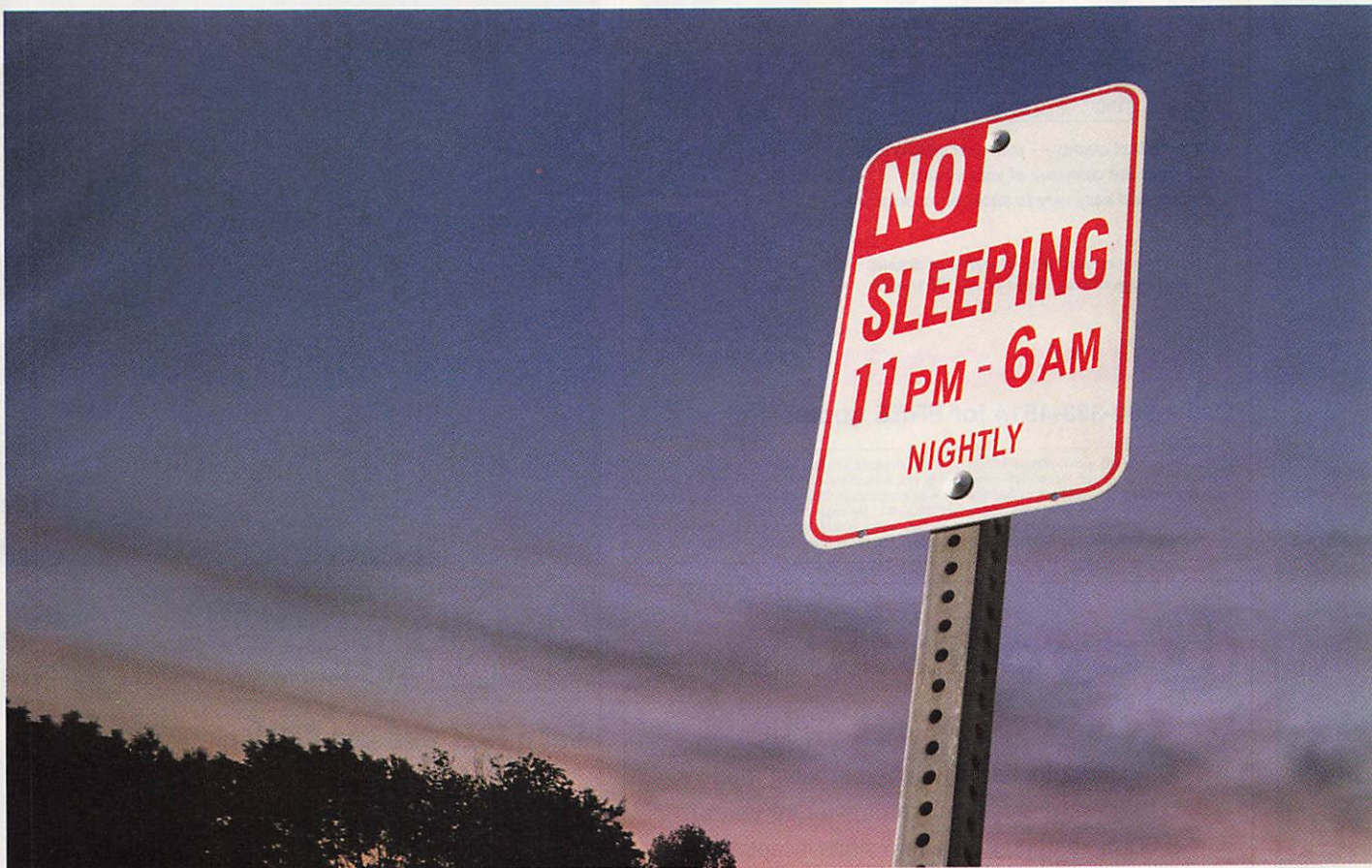
FUND AVERAGES

CATEGORY	TOTAL RETURN		
	ONE MONTH	ONE YEAR	THREE YEARS¹
Stock Funds			
U.S. diversified equity	4.0%	-6.2%	7.3%
Large-cap	3.6	-4.6	7.0
Midcap	5.8	-5.5	9.2
Small-cap	4.2	-12.2	6.0
Balanced	2.3	-1.9	6.4
Overseas	8.4	1.6	17.8
Bond Funds			
U.S. government	-1.9	6.0	3.7
Investment-grade corporate	-0.8	2.4	3.1
High-yield corporate	2.7	-3.7	4.4
Tax-exempt	1.0	0.6	2.6

TOP-PERFORMING FUNDS

CATEGORY	TOTAL RETURN ONE YEAR	THREE YEARS¹	EXPENSES (AS % OF ASSETS)
Large-Cap Stocks			
Janus Adviser Forty (JDCAX)	28.0%	21.6%	0.94
U.S. Global Accolade Global MegaTrends (MEGAX)	15.7	13.5	2.49
American Century Legacy Large Cap (ACGOX)	14.8	N.A.	1.10
Waddell & Reed Adv. Tax-Mgd. Equity (WTEAX)	13.6	13.1	1.31
Saratoga Large Cap Growth Portfolio (SLCGX)	13.3	14.0	1.53
Midcap			
CGM Focus (CGMFX)	66.2	36.1	0.99
Brazos Mid Cap Portfolio (BMCNX)	17.1	14.0	1.23
American Century Gifttrust (TWGTX)	16.4	23.9	1.00
American Century Heritage (TWHIX)	16.3	23.9	1.01
Janus Adviser Orion (JORAX)	15.9	N.A.	1.21
Small-Cap			
Prasad Growth (PRGRX)	13.7	6.4	1.50
Transamerica Small/Mid Cap Value (IIVAX)	11.6	16.7	1.41
Alpine Dynamic Innovators (ADINX)	11.1	N.A.	1.33
Royce Global Select (RSFTX)	6.0	N.A.	2.40
Eaton Vance Tax-Mgd. Small-Cap Growth (ETMGX)	5.2	16.6	1.34
Balanced			
CGM Mutual (LOMMX)	36.5	17.8	1.05
John Hancock Balanced (SVBAX)	16.1	17.2	1.28
Regions Morgan Keegan Select Balanced (FPALX)	9.5	10.3	1.26
Oakmark Equity & Income (OAKBX)	9.3	11.8	0.83
Northern Lights Arrow DWA Balanced (DWAFFX)	8.9	N.A.	1.83
International			
Fidelity Canada (FICDX)	22.4	25.4	0.94
Driehaus International Equity Yield (DRIYX)	17.6	N.A.	1.75
Amidex 35 Israel Mutual (AMDEX)	16.1	16.9	3.40
Allianz NFJ International Value (AFJAX)	15.1	25.2	1.46
Nationwide International Growth (GIGAX)	12.9	27.6	1.57
Emerging Markets			
ProFunds UltraEmerging Markets (UUPSX)	40.0	N.A.	2.38
Goldman Sachs BRIC (GBRAX)	33.5	N.A.	1.98
Dreyfus Emerging Markets Opportunity (SEOAX)	31.3	N.A.	1.95
Legg Mason Emerging Markets Trust (LMEMX)	29.0	37.2	2.25
RS Emerging Markets (GBEMX)	28.9	36.8	1.75
U.S. Government Bonds			
Direxion 10 Year Note Bull 2.5x (DXKLX)	25.8	6.5	1.75
Rydex Gov. Long Bond 1.2x Strategy (RYGBX)	10.5	3.9	0.97
ProFunds U.S. Government Plus (GVPSX)	8.8	2.2	2.22
Fidelity Government Income (FGOVX)	8.8	5.3	0.44
Pimco Long-Term U.S. Government (PFGAX)	8.5	4.6	0.88
Investment-Grade Corporate			
Target Total Return Bond Portfolio (TATBX)	10.5	6.2	0.64
Old Westbury Fixed Income (OWFIX)	9.8	5.5	0.73
Pimco Total Return (PTTAX)	9.8	5.6	0.90
Harbor Bond (HABDX)	9.7	5.7	0.56
Target Intermediate-Term Bond (TAIBX)	9.3	5.5	0.58
High-Yield Corporate			
Value Line Aggressive Income Trust (VAGIX)	1.7	5.4	1.04
Morgan Stanley High Yield Securities (HYLAX)	1.4	6.0	1.59
Principal High Yield II (CPHYX)	1.2	9.4	0.85
Pax World High Yield Bond (PAXHX)	1.0	6.2	1.13
Lazard High Yield Portfolio (LZHOX)	0.6	6.2	0.85
Tax-Exempt			
Baird Intermediate Municipal Bond (BMBX)	6.2	3.9	0.55
State Farm Municipal Bond (SFBX)	5.8	4.1	0.15
Marshall Intermediate Tax-Free (MITFX)	5.6	3.7	0.60
Fidelity Short-Intermediate Muni Income (FSTFX)	5.5	3.6	0.44
U.S. Global Investors Near-Term Tax Free (NEARX)	5.4	3.5	0.45

NOTES AND SOURCES: As of April 17 from Lipper, New York; 877-955-4773. Tickers represent the largest share class. The 10 Biggest Stock Funds are ranked by total net assets.¹ Annualized.² Closed to new investors. N.A.: Not applicable or not available.



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Health.com
Where to turn

Life insurance rates drop to all-time lows

Sample Monthly Rates

Age	\$500,000	\$1,000,000	\$2,000,000
35	\$13	\$21	\$37
40	\$17	\$28	\$52
45	\$27	\$46	\$88
50	\$38	\$68	\$132
55	\$55	\$101	\$196
60	\$82	\$151	\$298
65	\$130	\$246	\$487

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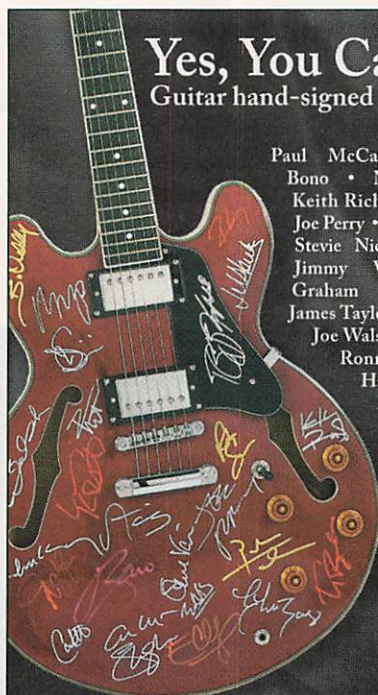
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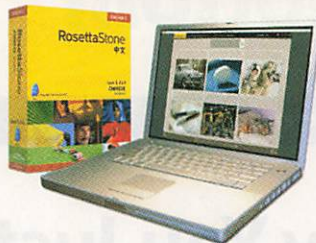
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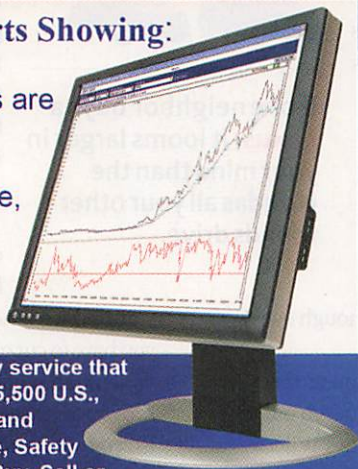


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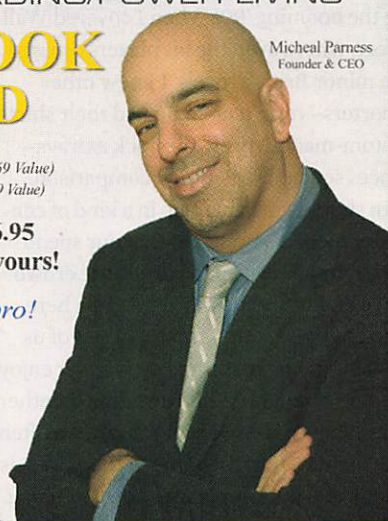
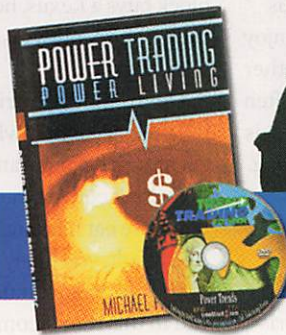
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BY PAT REGNIER

Why You Just Can't Seem to Save Enough

YOUR MORTGAGE IS PRIME. Your credit-card balance is reasonable. You've set aside some money for retirement. Feeling like you've done all you should?

Didn't think so. All signs point to an economic slowdown, and there's a real risk that it will be a nasty one. Jobs look shaky, food and gas prices are up, and the credit you thought would be there in an emergency could get a lot more expensive. Even if you've been better than the average American about saving, you probably wish that you had a bigger cash cushion right now.

And if you're at all like me, you've been looking around your house lately and wondering, "Why didn't I put the money I spent on *that* in the bank?" Seriously, there are shirts in my closet that would make Daisy Buchanan weep...and I get misty too when I think of the cash I wasted on them. What can I say? I bought them during the booming '90s when I covered Wall Street, where even the bit players dressed like minor British royals. I knew other reporters—*reporters*—who had their shirts custom-made. My off-the-rack extravagances seemed sensible by comparison.

In short, I got caught up in a kind of consumer mob. It's no secret that our spending habits are driven in part by the crowd we're in. But there's more going on here than envy and status seeking. Most of us don't like doing math, and even fewer enjoy keeping a budget. When deciding whether a big expense is reasonable or not, we often take mental shortcuts. One of the easiest is to look at what people we know are doing.

That's trouble because we're almost certain to draw the wrong conclusions, says Ronald Wilcox of the University of Virginia business school. His new book *Whatever Happened to Thrift?* is a surprisingly witty guide to a gloomy subject: the

complete inability of the world's richest nation to save. A big part of the problem, Wilcox says, is that our shortcut-loving brains trick us. "We tend to remember extraordinary consumption more than mundane consumption," he notes. Wilcox says this is an example of what research psychologist Thomas Gilovich calls a one-sided event. There's little reason to notice that most of your neighbors drive Accords. It's a good car, but who daydreams about owning one? When a single family on your block buys a Lexus, however, it suddenly feels as though everybody has one.

Our friends play tricks on us too. "We tell people about it when we go out to eat at a nice restaurant," says Wilcox. "We don't convey the same information when we eat mac and cheese at home." As a result, you likely have a skewed view of your friends' standard of living. Now add to this that incomes in America have grown increasingly unequal. A few folks



If one neighbor buys a Lexus, it looms larger in your mind than the Hondas all your other friends drive.

you know (and most of those you see in the media) really are doing better than you are, and that distorts your view even more. Wilcox calls the end result "perceived consumption superdisparity." It'll leave you superbroke if you aren't careful.

I asked Mary Claire Allvine, a financial planner in Chicago, if she had any tips for breaking free of PCS affliction. Cutting back on every little extravagance, like your morning tall skinny latte, won't get you very

far, she says. And it's hard to sustain. Better to simplify the problem. Instead of limiting your spending so you can save what's left, decide first what you'll save and learn to live on the rest. And get it out of your hands as fast as you can. Signing up for automatic withdrawals, through a 401(k) at work or in a taxable mutual fund account, will help you a lot.

Allvine offers more unconventional advice: If high-living pals are a problem for

you, find some new ones. That doesn't mean you have to cut off the big spenders. Just widen your social circle. Take up a volunteer activity or a cheap hobby where the accent isn't on consumption. Forget the country club. Join the "Y" or, better yet, an investing group with a long-term focus.

And avoid reporters in custom shirts. They'll probably hit you up for a loan. **\$**

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the
away.”
report #11237

our lawn and
our newspaper.”
- member report #12737

very envious
neighbors.”
- member report #1456

Both times.”
- member report #5678

was a miracle
worker...”
- member report #10100

is in good
hands.”
- member report #47872

when they
show up.”
- member report #12342

re was
I was
ng?”
report #9321

“Their
reputation is
as spotless as
their work.”
- member report #5178

“He’s a
cat hater.”
- member report #11222

“Don’t
expect him to
negotiate.”
- member report #3462

“No pressure.
Just honest and
professional.”
- member report #4160

“...the price was
excellent given
the detail
involved...”
- member report #11454

“It’s a shame
we only see him
when something
breaks.”
- member report #8165

whole
was a
ght.”
report #8767

“A fence
even a neighbor
could love...”
- member report #10101

“We kicked
them out before
something else
happened.”
- member report #3425

“I wish every
home project
would go this
smoothly.”
- member report #2319

“My wife
wanted him to
stay for dinner.”
- member report #17852

“He respected
my time, opinion
and privacy.”
- member report #1313

“Absolutely
outstanding.”
- member report #2011

cordial,
hly
etent.”
report #1273

“They
worked like
bees and did an
excellent job.”
- member report #7371

“What a mess!”
- member report #1737

“...clean shaven
and most
professional
looking...”
- member report #2737

“Made me feel
like I was their
only client.”
- member report #9832

“There
was a very
hard language
barrier...”
- member report #4567

“Went to small
claims court –
we won.”
- member report #1099

eserves
edal
ience.”
report #996

“...it was also
tough to get
the deposit
back.”
- member report #2636

“...they were
Johnny on
the spot...”
- member report #7477

“I can’t believe
how great it
looks and how
inexpensive
it was.”
- member report #9273

“They did it
in just a couple
of days.”
- member report #13772

“They will help
you lift things
out of your car
and so on.”
- member report #12222

“...not the
electrician to
call if you
have pets.”
- member report #1313

his
pany
atched
my of
ers...”
report #8345

“Grandpa did
the estimate...
Pa and son did
the work.”
- member report #5789

“I had to hire
someone else
to redo half
the job.”
- member report #10232

“They were
here two hours
and charged
me \$840.”
- member report #9323

“...make sure
you ask for the
discount...”
- member report #11357

“We waited
almost two
weeks for our
appointment.”
- member report #6783

“He treated
my house like it
was his own!”
- member report #4592

stallers
ed the
time.”
report #852

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as no
n using
s like
you.”
report #5678

“...he couldn’t
have been more
disinterested
in the job...”
- member report #31257

“These
employees love
what they do
and it shows.”
- member report #6942

“I offered to pay
him something
additional, but
he refused.”
- member report #6543

“They never
showed up and
never called...”
- member report #8765

sed our
ment
sons
ound
ble...”
report #11789

“Got the
response
‘I don’t know’
a lot.”
- member report #15672

“...quote was
reasonable and
the actual price
was lower.”
- member report #6479

“The workers
were an hour
late, but did
great work.”
- member report #8900

“They
were friendly,
and even let
my daughter
pretend to
help.”
- member report #31455

“...destroyed
part of my lawn
by leaving
equipment
on it...”
- member report #8721

“He understood
because he has
kids of his own.”
- member report #6521

e work
leted...”

“A first
class job by first

“...the whole
place turned

“The end result
was first rate—
cosmetically

“...great quality
and attention

“She did
not charge

“...he even
helped me
with a ‘word

“...he even
helped me
with a ‘word